# PUBLISHED ACCOUNTS

## Their Construction & Criticism

BY

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# PREFACE

This study is the outcome of several years' patient research into the subject of published accounts of Indian companies issued after 15th January 1937 when the Indian Companies (Amendment) Act of 1936 came into force. Some five hundred actual published accounts of different companies have been minutely examined for the purpose of this research. The Amending Act of 1936 introduced some very material improvements in the form of published accounts; and an attempt has been made to examine the implications of the various statutory requirements affecting the published accounts and to discuss the different ways in which the letter of the law is being complied with in actual practice.

The book deals with the subject of published accounts under two headings, namely, the construction of published accounts (Chapters 1–7) and the criticism of published accounts (Chapter 8). As far as the subject-matter of this book is concerned, I have endeavoured to break new ground. There are some excellent books on Advanced Accountancy; but so far as I know there is none on this special branch of company accounts. The accountancy profession is growing fast in this country, and there appears to be a definite need for a book of this kind both for the use of accountancy students and practising accountants.

Since 1940 this country has been witnessing a great company boom, and the question of company accounts has therefore assumed a special significance from the point of view of those who have put in their money in the newly-born companies. It is earnestly hoped that this book will be found useful not only by company accountants and company managements but also by the ever-increasing class of investors in company shares and debentures.

The various sources from which any information is taken have been duly acknowledged in the text of the book; but I owe a special debt of gratitude to "*Commerce*" and "*Indian Finance*", from which I have learnt a good deal about the subject of published accounts and from which a lot of material has been taken for inclusion in this book. I am also deeply indebted to those managing agents who, at my request, supplied me with the published accounts of companies under their control without which it would have been impossible for me to undertake this piece of research.

Nawalgarh (Jaipur)
*6th February 1946*

R. R. G.

P. S.—It is stated at the bottom of page 2 that the relevant provisions of the Indian Companies Act of 1913, which have any bearing on the published accounts of companies, will be reproduced in Appendix A. But, as the size of the book has grown too large, this idea has been abandoned.

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# CHAPTER I.

## PUBLICATION OF ACCOUNTS.

The existing law of companies is found in the Indian Companies Act as passed in 1913 ( Act VII of 1913 ) and as amended from time to time since then and as thoroughly overhauled by the Indian Companies ( Amendment ) Act of 1936.

The Act VII of 1913 remained in force practically in its original shape for nearly a quarter of a century, and during all this time it was found to be defective in many respects The plea for reform had been urged for years and years. It had been put forward from diverse and even differing platforms The Shareholders' Association in Bombay and the *Indian Finance* in Calcutta had cried themselves hoarse that reform in company law was imperative and urgent. In his last Cotton Textile Report, Dr. John Matthai had stressed the importance and urgency of company law amendment. Even the Federation of Indian Chambers of Commerce and Industry, which may be regarded as a zealous guardian of capitalist rights and prerogatives, had passed resolutions favouring early investigation of company law. A large and authoritative section of public opinion was firmly persuaded that the capital market in India would continue to remain taciturn and even hostile to new enterprises until and unless company law was so changed as to afford the public a sense of security that there was an alert watch dog in the shape of the State which would track down all offenders and criminals in company management. Indian industrial advancement, which had come to a standstill owing, in some cases, to the vagaries of directors and managing agents, stood in urgent need of timely and powerful stimulus. Such stimulus could be afforded only by a company law which satisfied public conscience that the arm of the law would come heavy and severe upon all evil-doers. From this point of view, the future of industrial progress was bound up with the overhaul of company law. (*The Indian Finance*, dated 14th December 1935.)

As a result of this movement for company law reform the Government of India had received substantial material in the form of communications and suggestions from local governments, public bodies and individuals, supplemented by publications in the press, indicating unanimity of opinion that the Indian Companies Act of 1913 required fairly extensive changes. The opinions received disclosed a demand for power to deal with mushroom and fraudulent companies, for changes in the provisions relating to the issue and contents of prospectuses, for increased disclosure to shareholders of the financial position of companies and for increased rights to shareholders in connection with the management of companies, for modification of the present law applicable to managing agents, for changes in the provisions applicable to winding up, for special

provisions to govern banking companies and for numerous other improvements.

In September 1934 the Government of India had placed on special duty a lawyer with experience in the administration of company law in order to examine the material collected and to make proposals for the amendment of the company law. The Special Officer's proposals embodied in his report submitted in 1935 were further considered by a small Advisory Committee consisting of business experts. Out of these proposals and discussions emerged the Indian Companies ( Amendment ) Bill of 1936, which, after being revised by the Select Committee, was placed before the legislature at the end of August 1936. The Amending Bill was passed into law in October 1936 and came into force on 15th January 1937.

The Amending Act ( Act XXII of 1936 ) brought about extensive changes ( particularly with regard to the published accounts of companies ) in the Indian Companies Act of 1913. Our company law has closely followed the English company law, and the Amending Act of 1936 was in some measure due to the lead given by the English Companies Act of 1929. It is, however, interesting to note that although we have modelled our company law on the English company law yet we have tried to avoid the shortcomings of the latter, and the result is that our law is in many respects in advance of the English company legislation We have been thus benefited from the experience of the administration of the English company law. When the Indian Companies Amendment Act of 1936 had been passed, it was felt by some people in England that this country had overlegislated in the matter of companies, and that it would have been advisable to leave at least the form of published accounts to shareholders and public opinion, as is the case in that country. ( *The Accountant*, dated 27th April 1937. )

The term 'Published Accounts' refers to the summaries of the accounts of public limited companies which are made available to the public. Private limited companies are not required to publish their accounts.

There is no legal obligation on a private business owned by a sole trader or a partnership to publish any accounts or even to keep any accounts at all. Insolvency Acts however, impose a severe penalty upon a trader, who, having been declared insolvent, had failed to keep proper accounts prior to the date of the presentation of the insolvency petition. This provision indirectly compels a trader to keep accounts. In the case of a company incorporated under the Indian Companies Act, there are, however, definite provisions relating to the keeping of proper accounts, the publication of periodical summaries thereof, and the submission of these to the members of the company for their approval. Since the control of such companies is practically divorced from the ownership of the shares, accurate accounts are necessary to enable the proprietors of a company to see the result of the activities of the directors and managing agents whom they appoint to manage the business in which their funds are invested. The law has recognised this need, and has provided accordingly.

The relevant provisions of the Indian Companies Act of 1913, which have any bearing on the published accounts of companies are

reproduced in Appendix A *to this book*; and the sections referred to are the sections of the Indian Companies Act of 1913 unless otherwise stated. Apart from the statutory requiremeots the articles of association of a company may also contain certain provisions relating to acconnts. The statutory provisions governing the pnblication of the acconnts of companies will now be considered.

## (A) BOOKS OF ACCOUNT.

The provisioos of the Act with regard to the keeping of books of account are cootained in section 130 and regulation 105 of Table A which regolation is compulsory in the case of all compaoies. Every company must keep proper books of account for recording.

*(a)* All sums of money received and paid by the company and the matters in respect of which the receipt and payment take place ;

*(b)* All purchases and sales of goods made by the company; and

*(c)* The assets and liabilities of the company.

The law does not prescribe any particular system of bookkeepiog ; nor does it lay down any particnlar language in which the accounts sbould be kept. The books of acconnt may be kept according to tbe Engllsh system of accountancy or the Indian system of Bahl-khata ; bnt the accounts are generally maintained in English and according to the English system of bookkeeping. Very few companies keep their accounts in vernacular.

The books of acconnt are to be kept at the registered office or at such otber place as the directors think fit.

Where a company has a branch office, proper books of acconnt relating to the transactions effected at the braoch may be kept at the branch office; but proper summarised retnrns, made up to dates at intervals of not more than two months. must be sent by the branch office to the head office for incorporation In the principal books of acconnt.

The responsibility for keeping proper books of accounts is imposed on managing agents, and where there are no managing agents, oo the directors, any default being penalised by a fine not exceeding one thousand rupees.

The books of account shall be open to inspection by the directors during business hours ; and by regulation 105 of Table A the members are also entitled by a resolution passed in general meetiog to inspect the books of account. It is a very valuable right of the members that they can iospect the books of acconnt of the company by passing ao ordinary resolutioo at a general meetiog, because by doiog so they may sometimes secure usefol results, particolarly if the affairs of the company are being mismanaged.

## (B) LAYING ACCOUNTS BEFORE GENERAL MEETING.

The directors of every company are reqoired by sectioo 131 (1) to lay before a general meeting of members in each calendar year

a balance sheet and a profit and loss account (or an income and expenditure account in the case of a company not trading for profit). The balance sheet and the profit and loss account are known as accounts or a statement of accounts. The first accounts must be presented at some date not later than eighteen months after the incorporation of the company, and the subsequent accounts must be presented once at least in every calendar year.

The accounts must be prepared for the period from the date of incorporation in the case of the first accounts and from the date of the preceding accounts in any other case up to a date not more than nine months (or in the case of a company carrying on business or having interests outside British India by more than twelve months) prior to the date of the meeting at which they are presented. These periods of nine or twelve months may be extended by the Registrar for any special reason by a period not exceeding three months.

Thus a company formed on, say, 15th June 1944 must present its first accounts at a meeting not later than 15th December 1945. If they are presented at this latest date, they must be made up to a date not prior to 15th March 1945, or if the company has interests outside British India, not prior to 15th December 1944.

Theoretically we say that a balance sheet is prepared on a particular date and a profit and loss account for a particular period. But the two accounts taken together are referred to as being prepared for a certain period, e. g., the accounts of ........................ Co, Ltd., for the year ended 31st March 1945

**Prompt Accounts.** It will be seen from the above that the accounts of a company may be laid before the general meeting as long as nine months (and sometimes twelve months and even longer) after the date to which they are made up. If the members are to be able to make any real use of the accounts, the accounts must be before them soon after the close of the financial period. Generally speaking three months should be sufficient for the preparation, audit and publication of accounts. Some companies, indeed, have their accounts produced in a matter of weeks. If the affairs of a company are in order, the time limits are unnecessarily generous; while if things are going badly and the directors take full advantage of the maximum time limits, they have had far too much latitude. Nine months after the accounting date is no time to be considering a loss and to be listening to the assurances of the chairman than the results are now believed to be satisfactory.

A general meeting of a company is a meeting of its members. But who is a member; who is entitled to receive notice of a general meeting; and who is entitled to attend, speak or vote at a meeting?

**Who is a member?** The term 'member' is carefully defined in section 30 by which two distinct things are necessary in order to make a person a member of a company, namely,—(i) That person must have agreed to become a member of the company, and (ii) His name must be on the register of members.

A person agrees to become a member in three ways :- In the first place, section 30 provides that every person who signs the memorandum of association shall be deemed to have consented to become member; secondly, every applicant for an allotment of shares, whose offer is accepted before it has lapsed or been revoked, consents to become a member; and thirdly, every person who agrees to take a transfer of shares from a member consents to become a member.

The latter requirement is just as important as the former. A person who agrees to become a member does not become a member until his name is put on the register of members.

The term shareholder' does not possess the same meaning as the term member. The person who holds a share warrant payable to bearer is a shareholder. But he is not a member because his name does not appear on the register of members. Again the legal representative of a deceased or insolvent member is not a member until he applies to the company for registration as a member, although he is a shareholder even without being placed on the register of members. The term member does not necessarily include every shareholder. Moreover, in, the case of guarantee companies not having share capital, it includes people who hold no shares at all.

**Who is entitled to receive notice of a general meeting?** According to regulation 116 of Table A, which is compulsory for all companies, notice of every general meeting shall be given to every member of the company (including bearers of share warrants) except those members who (having no registered address in British India) have not supplied to the company an address within British India for the giving of notices to them, and also to every person entitled to a share owing to the death or insolvency of a member.

If a member has no registered address in British India, and has not supplied to the company an address within British India for the giving of notices to him, a notice addressed to him and advertised in a newspaper circulating in the neighbourhood of the registered office of the company shall be deemed to be duly given to him on the day on which the advertisement appears.

It means that notice of a general meeting is to be given not only to every member but also to certain non-members such as the bearers of share warrants and the legal representatives of a deceased or an insolvent member.

**Who is entitled to attend, speak and vote at general meeting?** Although all members and some non-members have a right to receive notice of a company's general meeting, yet they all do not enjoy the right to attend, speak or vote at that meeting Of course, no non members such as the bearers of share warrants or the legal representatives of deceased or insolvent members are ordinarily allowed this privilege. But the articles of most companies impose restrictions even on the members themselves in respect of the right to attend, speak or vote at general meetings. The following are the typical restrictions inserted in the articles of companies :—

1. No member is entitled to be present or vote on any question either in person or by proxy or as proxy for another whilst any call or other sum shall be due and payable to the company in respect of any of the shares of such member.

2. Any member who shall change his name or place of abode shall not be entitled to recover any dividend or to vote, until notice of the change of name or abode is given to the company in order that the same be registered.

3. Every member not disqualified and who has been duly registered for three months previous to a general meeting (but not otherwise) shall be entitled to be present and speak at such meeting.

4. The holders of preference shares are entitled to be present at any general meeting with the permission of the chairman. Preference shares confer the right to vote at a general meeting only when the dividend on such shares is in arrears for twelve calendar months or when any resolution is proposed for reducing the capital of the company or winding up the company or directly affecting the interest of holders of such shares as a class as regards dividend, return of capital or voting. Upon any question which entitles the holders of preference shares to vote, these shares shall confer one vote for each share held.

## (C) AUDIT OF ACCOUNTS

Under section 131 (2) it is necessary that the balance sheet and the profit and loss account of a company should be audited by the auditor of the company. The auditor's report should be attached to the accounts or there should be inserted at the foot thereof a reference to the report, and the report should be read before the company in general meeting and should be open to inspection by any member of the company.

The auditor's report may be attached to the accounts or it may be a separate document, a reference to which being made on the accounts. There is, however, no point in making the auditor's report a separate document when a copy of it is to be circulated to every member and is also to be filed with the Registrar. In practice, therefore, the auditor's report is always given on the accounts.

## (D) AUTHENTICATION OF ACCOUNTS.

Section 133 provides for the signing of balance sheet and profit and loss account or income and expenditure account as the case may be. In the case of banking companies they should be signed by the manager or managing agent, and where there are more than three directors, by at least three directors, and where there are not more than three directors, by all the directors. In the case of other companies, the accounts should be signed by at last two directors, or where there are less than two directors, by the sole director, and also by the manager or managing agent of the company

If, for any reason, the total number of directors present in British India at the time when the signature of the directors is required is less than the number required, the accounts should be signed by all the directors for the time being in British India. If at the time there is only one director present in British India, the accounts are to be signed by such director alone. In every case a statement, signed by the director or directors signing the accounts, must be appended to the accounts explaining the reasons why the accounts could not be signed by the required number of directors.

## (E) CIRCULATION OF ACCOUNTS.

Under section 131 (3), every company, other than a private company, is required to send a copy of the audited balance sheet and profit and loss account (or income and expenditure account) together with a copy of the auditor's report to every member at *his registered address*, at least *fourteen days before* the meeting at which they are to be presented. The period of 14 days is intended to give the members an adequate opportunity for considering the accounts.

Section 146 gives the holder of preference shares and debentures and also the trustees for debenture holders of a public company the same right to receive and inspect copies of the balance sheet and profit and loss account of the company together with the reports of the auditors and other reports as is possessed by the ordinary shareholders. That is to say, such persons can demand the accounts and reports gratis, but the company is not bound to supply them without asking.

Under section 135, the members of a private company are also entitled to be furnished with copies of the balance sheet and the *profit and loss account* and the *auditor's* report on payment of six annas for every hundred words to be copied.

## (F) CONSIDERATION OF ACCOUNTS.

The members of a company appoint the directors and the managing agents to conduct the affairs of the company on their behalf. It is, therefore, necessary that the directors should render from time to time to their principals (i. e., the members) an account of their stewardship. For this purpose, the law makes provision for the periodical calling of company meetings.

Under section 76, the directors of a company must call the first ordinary general meeting within 18 months of the date of its incorporation, and subsequent ordinary general meetings must be called once at least in every calendar year and after an interval of not more than 15 months after the last preceding ordinary general meeting.

An ordinary general meeting of a company is held for the purpose of laying before the members for their consideration and approval the accounts of the company and also for transacting any

other ordinary business as specified in the company's articles. This also gives the chairman of the company an opportunity of explaining the operations of the company, and of answering any questions which the shareholders may ask and which he may see fit to answer.

The accounts of a company, a copy of which has already been circulated to the members, are laid before the ordinary general meeting, and, after being considered by the members, are either adopted or rejected. The usual procedure at an ordinary general meeting is for the chairman to address the meeting on the company's operations for the period covered by the accounts, to explain the leading features of the accounts, and sometimes to give an indication as to how the company is faring during the current year, and possibly to indulge in some mild prophecy. He then moves that the accounts be adopted. The chairmen's motion having been seconded, it is usual for him to invite questions from members. It is then that the dissatisfied members not only ask questions but also ventilate their views on the manner in which the company's affairs are directed and make suggestions for the consideration of the management.

Members who are thoroughly dissatisfied with the management will sometimes take the extreme course of rejecting the accounts. Such a course however, can have little or no practical effect unless it is accompanied by the appointment of a committee to investigate the affairs of the company, and an adjournment of the meeting until the committee has reported the result of its investigation.

When all is well, and profits are ample and progressive, company meetings are usually happy functions, at which there are smiles and mutual congratulations all round But when all is not well, and members suspect that there has been mismanagement on the part of directors and managing agents, a company meeting may be anything but a happy gathering. Members who have been deluded into losing their money are usually angry and often voluble It is seldom that scattered or unorganised criticism achieves much at a company meeting. The most effective means of dealing with recalcitrant or incompetent directors is to organise opposition, to collect proxies, and to leave the talking to practised and experienced speakers (Kissan & Williams: *Investment in Stocks and Shares*).

Where the accounts of a company laid by the directors before a general meeting are unsatisfactory, where dividends have not been received for some years, where the explanations given at the meeting are not entirely satisfactory, or where the information as to the proximate causes of the present financial position of the company is refused—the members have a theoretical right of rejecting the accounts and appointing a committee to investigate the affairs of the company. But in practice such a course is impossible in ninety-nine cases out of a hundred for the following reasons:—

1. The directors and managing agents have a shareholding sufficient to give them a controlling interest; or even if they have not, they can rely upon the apathy of a sufficient number of members, whereby they abstain from attendance at company meetings. It is

also well-known that there is always a large section of the shareholders who, for diverse reasons, will always support the board or who are content to appoint one or other of the directors as their proxies.

2. The vast majority of the shareholders of a company have neither time nor ability nor inclination to regard these concerns in any other light than as mere agencies for the production of surplus value. Shares in industrial enterprises come to be mere certificates of claim to receive dividends, saleable at a stock market value varying with business conditions and with the anticipated fortunes of each particular enterprise. Their owners, entitled to attend the company meetings and therewith by their votes to supervise the management of their businesses cease in most cases even to consider the possibility of attendance, or to regard themselves as in any way responsible for the conduct of the enterprises which are legally their property This is natural and Inevitable; for what collective influence can possibly be exercised by a constantly shifting body of shareholders, scattered far and wide, unknown one to another, and for the most part utterly ignorant of the conditions of the industry or the business in which their money is embarked? Investors nowadays habitually buy and sell, in their own minds, not shares in the ownership and responsibility of a shipyard, or a steel works, or a chemical factory, but claims to receive from theses enterpries an income, which may turn out well or ill. Occasionally, a scandal or a scare attaching to a particular company may attract a large attendance at a general meeting; but as a rule the great majority of shareholders no more think of attending a meeting than an atheist thinks of going to church. (G. D. H. Cole: *Socialism in Evolution*).

This state of affairs, viz.—that the members of a company, legally entitled to supervise the management of its affairs, cannot in practice always do so—is not generally prejudicial to their interests. In the majority of cases, the system works quite satisfactorily where the management is good and responsible. It is well-known that legislature has refrained, as far as possible, from introducing legislation which would have the effect of hampering the internal organisation of companies. They have taken the view that generally a company must be left to govern itself; and the members have been given sufficient safeguards against possible frauds and mismanagement.

## (G) *FILING OF ACCOUNTS.*

Section 134 requires every public company to file with the Registrar three copies of the balance sheet and profit and loss account after those accounts have been laid before the general meeting. The copies to be filed must be signed by the manager or secretary of the company and filed within 21 days after the day of the first or only ordinary general meeting in the year.

If the general meeting before which the accounts are laid does not adopt them, a statement of the fact and of the reasons therefor must be annexed to the accounts and to the copies thereof required to be filed with the Registrar.

Where the Registrar on perusal of any document which a company is required to submit to him, is of opinion that any informa-

tion or explanation is necessary in order that such document may afford full particulars, he may, under section 137, by a written order call upon the company to furnish such information or explanation and within such time as he may specify in his order. On receipt of such an order it shall be the duty of all persons who are or have been officers of the company to furnish such information or explanation to the best of their power.

On receipt of such information or explanation the Registrar may annex the same to the original document submitted to him; and any additional document so annexed shall be subject to the same provisions with regard to inspection and the taking of copies as the original document.

## CHAPTER 2.

### THE BALANCE SHEET (1)

A balance sheet is a classified summary of all the balances remaining in a set of books after those relating to profit and loss have been collected together in an account called the Profit & Loss Account. It includes the balance of the profit and loss account as well along with other balances. It is arranged in such a way as to show the assets and debit balances upon one side, and the liabilities and credit balances upon the other. It represents the culmination of the system of bookkeeping, and should be a document setting forth the true position of the business in such a manner as may be easily understood by men of business intelligence. (Spicer and Pegler : *Practical Auditing*)

The terms "assets and debit balances" and "liabilities and credit balances" are important, as they at once indicate that some things are included which are neither assets nor liabilities. The liabilities and credit balances appear on the left-hand side of the balance sheet and the assets and debit balances on the right hand side. Thus the items appear in the balance sheet on the side opposite to that on which they appear in the ledger accounts.

The balance sheet is a statement that is prepared at the end of a trading period, and is headed as being on such and such a date.

It is the shareholder's or investor's quick guide to the financial position of the company. It tells him whether the enterprise is solvent and whether it is well situated for the achievement of prosperity and profit. An ideal balance sheet will show at a glance not only, as it professes, the assets and liabilities, but also the true nature of each. If, for example, a company has machinery which is outmoded, or if it has a modern plant which is idle because floating capital is not present to feed it with its raw materials, the assets so represented are realisable perhaps, but are not of much profit earning value at the date of the balance sheet. It must, in this connection, be borne in mind that a balance sheet can never be more than a summary of the company's books. It gives the balances of the various accounts, and it may fuse together one or more of them, and unless there is some indication of the realities behind the accounts it will be of little value to the reader. (W. C. Brooks: *Theory and Practice of Finance*)

With regard to the balance sheets of limited companies, there is need for a clear and informative exposition to the shareholders who have invested their money but who are not in a position to influence to any extent the conduct of affairs There are, however, many members of the investing public to whom any form of balance sheet, however informative it may be, would be of the nature of a Chinese puzzle. Therefore persons interested in company balance sheets must be

sufficiently acquainted with commercial terminology and usages to understand the fundamentals.

It is a little astounding and one cannot help wondering whether those who manage big companies do not forget sometimes that the body of directors of a company are the agents and the trustees of the shareholders, that they owe them full information, subject to proper and reasonable commercial necessity; they owe them full information, and it is their interests that they have to study; they are not to regard shareholders as people who may look up if they are not fed; they are the people whose money they are using, and it is to be remembered that a joint stock company is a creation of law.

A joint stock company has the enormous advantage of limited liability and the legislature has intended to secure that those who enjoy those privileges of limited liability and who control and manage joint stock companies should be subject to some condition as to publishing their accounts at least to the shareholders and at least to those who are entitled to be summoned to general meetings.

**Statutory Contents of a Balance Sheet.** The law relating to the balance sheet of a company other than an insurance company is contained in sections 132 (1) and (2) and 105 B. The contents of the balance sheets of insurance companies are laid down in the Indian Insurance Act of 1938.

Section 132 (1) requires that the balance sheet shall contain a summary of the property and assets and of the capital and liabilities of the company giving such particulars as will disclose the general nature of those liabilities and assets and how the value of the fixed assets has been arrived at; while section 132 (2) prescribes that the balance sheet shall be in the form marked F in the Third Schedule to the Indian Companies Act of 1913 or as near thereto as circumstances permit.

The Indian Companies Act prescribes a definite form of balance sheet, which the English Act does not. By being placed in the Third Schedule, the balance sheet falls within the category of forms which can be modified by notification of the Governor-General in Council, as provided by section 151 (2).

The keynote of a balance sheet is 'information' within certain limits and not 'concealment'. The clear provisions of the law as to the form in which the balance sheet must appear, viz.—form F in the Third Schedule, cannot be allowed to be whittled down by general considerations as to the object of a balance sheet. (1927. *Re Central Bank of India, Ltd.*, Bom. L. R. 722).

A balance sheet must not be a mere inventory, but must be in the nature of a pictorial representation of the trading position of the company easily appreciated not by ignorant people but by persons reasonably able to understand commercial expressions and commercial conditions. (The Hon'ble Mr. Justice Cunliffe in *Superintendent and Remembrancer of Legal Affairs, Bengal v. Akhil Bandhu Guha and Other, 1936)*

The legal requirements with regard to a company balance sheet may be summarised as follows:—It must be as far as possible in the prescribed form; it must disclose the general nature of liabilities and assets; it must disclose how the value of the fixed assets has been arrived at; and it must comply with the provisions of section 105B.

It is now proposed to consider in detail the requirements of Form F in the Third Schedule.

## I. SHARE CAPITAL.

Every company requires capital for two purposes: (1) Capital for Block, that is, to finance fixed assets and expenses of organisation, and (2) Working capital, that is, to finance floating assets. Block capital is required by newly started companies for fixed assets, such as land, buildings, machinery and other appliances of a durable and permanent character. It is also required in the case of established companies for purposes of extensions and improvements The capital that is invested in these fixed assets is more or less of the nature of permanent investment.

Working capital is required for the purchase and working up of raw materials Into finished products, for stores, for expenses incidental to the marketing of products, for financing outstandings in respect of goods supplied, and for providing the necessary funds for meeting day to day requirements. The capital that is invested in this way should be of the nature partly of permanent or long-term capital and partly of short-term finance. The stock of raw materials and manufactured or semi-manufactured commodities never falls below a certain minimum and therefore the capital required for holding these is of the nature of permanent capital. Any working capital over this minimum falls under the category of short-term finance.

With regard to the capital plan of a company, the questions to be considered are the amount of capital required and the form in which it should be raised. The amount of capital needed is calculated by preparing detailed estimates of the block and working capital requirements.

When the amount of capital required has been estimated, the next thing to consider carefully is the form in which it should best be raised. The necessary capital may be obtained by means of shares (either of one class or of several classes such as preference, ordinary or deferred), debentures and/or public deposits. What factors determine the class or classes of shares to be issued, or as to whether a portion of the capital should be raised by debentures or public deposits? The factors regulating this question are feasibility, comparative cost, the desire to concentrate the control of the company in certain hands, the purpose for which the capital is required, and the state of the security market at the time.

Of course, the necessary capital should, if possible, be raised by the issue of securities of different classes such as preference shares, ordinary shares and debentures in order to cater for as large a number of investors as possible; but all companies are not in a position to do so. Preference shares can be issued only by those companies whose earnings are almost assured e. g, jute mills, sugar mills, public utility concerns and the like. Again, before a company can issue debentures, it must possess sufficient tangible assets acceptable to the debenture-holders as security, and these assets must be unencumbered and available for this purpose. Further there must be a reasonable prospect of the company being able to pay debenture interest out of

current income. Where the business of a company is of a speculative nature or liable to acute fluctuations, or has not yet been established on a revenue-earning basis, a large proportion of the capital, preferably the whole of it, should be in the form of ordinary shares.

The state of the security market has also to be taken into account. It sometimes happens that the investing public is anxious to invest safely; at other times the general desire is to obtain shares which offer the possibility of high return and capital appreciation. In times of depression, with money rates low, a debenture issue is much more likely to be successful than a share issue. Moreover debentures can then be issued at low rates which will be of distinct benefit to the company when trade revives. When a trade boom is in progress and the profits in the industry and of the company are high, shares can be issued often at a high premium. In such circumstances, it would be a bad policy to issue debentures for these would have to be given current high interest yields, which would create a severe burden when business activity declined and interest rates fell.

Sometimes the capital structure of a company is so designed as to concentrate control in the hands of a group of individuals. It may be that the company is being formed to acquire an existing business and additional capital will be required for development. If the vendors are to be the persons responsible for the conduct of the company's affairs, they may not themselves be in a position to provide these funds and they must therefore make an appeal elsewhere. They naturally do not wish to share the control with others if it can be avoided, and consequently decide to issue preference shares carrying restricted voting rights. A good many investors are quite satisfied to sacrifice such rights in return for the advantages as to dividends and/or return of capital which preference shares usually enjoy. A similar course is also sometimes adopted by promoters who are not slow to take advantage of the opportunity of controlling large concerns with a minimum use of their own funds. This is secured by issuing deferred shares of small value carrying disproportionate voting rights.

## CLASSES OF SHARES

The amount of capital which a company may raise by means of shares is stated in its memorandum of association, in which the number of shares into which such capital is to be divided is also mentioned. But the classes into which the shares are to be divided are fixed by the company's articles of association. It is not necessary that all the shares a company is authorised to issue should be so classified. Some of them may be classified and some may be left unclassified to be issued as a particular class in future by the directors of the company. An example of such unclassified or non-categorised shares is furnished by the Dunlop Rubber Co. (India), Ltd

The three principal classes of shares are preference, ordinary and deferred shares, but there may be several variations of them The respective rights and privileges of each class of shares of a company are found in its memorandum and/or articles of association.

## I. PREFERENCE SHARES

These are shares that carry with them certain preferential rights in priority to other classes of shares. That is why they are called preference shares. The several rights and privileges attached to preference shares may be as follows :—

1. **Dividends** The preference shares have a prior right to a fixed dividend, *i. e*, dividends on other classes of shares are deferred until the fixed dividend is paid on the preference shares. Unless the articles provide to the contrary, preference share dividends must be paid less tax; the declaration of free of tax dividends would deprive ordinary shareholders of profits to which they are entitled.

The fixed dividend on preference shares may be paid yearly or half-yearly. The existence of profits sufficient to pay the fixed dividends does not, of itself, give preference shareholders a claim to snch dividend. If in the directors' discretion it would seem that allocations to general reserve or other purposes are in the best interests of the company, they are justified in passing the preference dividend, or recommending its payment *in part only*. But directors must act in the interests of the company as a whole; any attempt to defeat the claim of preference shareholders by this means would be nullified if the members concerned obtained an injunction restraining them from disposing of profits in the proposed manner.

Preference dividends may be paid in a year when a loss has been incurred, provided nndivided profits carried forward from previous years are adequate to meet the payment, that is to say, a sufficient balance of past profits remains for the payment of the preference share dividend after making good the current year's loss. The South Behar Sugar Mills, Ltd., incurred a loss of about Rs. 1½ lakhs in the year ended *31st October 1943*, but it possessed reserves of over Rs. 5 lakhs built up out of past profits. It therefore declared dividends on preference, ordinary and deferred shares for that year out of past profits without regard to the current year's loss. On the other hand, preference share dividend may be paid out of current year's profits without making good past losses. The Hukumchand Jute Mills, Ltd., out of its profits for the half-year ended 30th September 1943, paid 7% cumulative preference share dividend absorbing Rs. 2,80,000, although it had on its books an accumulated past loss of over Rs. 5½ lakhs which was carried forward to the next half-year.

The dividend attached to preference shares may be cumulative non-cumulative or partly cumulative and partly non cumulative. If the preference share dividend is cumulative and if it is not paid in full in any one year or for a term of years, it must be paid up in full before the other shareholders can share in the profits. But where the preference share dividend is not cumulative, it extends only to each year or sometimes each half-year of the company's working. Accordingly preference shares are known as cumulative or non cumulative preference shares. The preference share dividend is usually cumulative.

The preference shares issued by the Khas Kajora Coal Co., Ltd., carry the right to a fixed cumulative preferential dividend of 5 per cent. per annum and to a non-cumulative dividend of 3 per cent. per annum,

Sometimes dividend on preference Shares may be paid out of capital under the provisions of Section 107.

2. **Repayment of Capital.** Almost invariably preference shares carry the additional right to a return of capital in priority to other classes of shares; but this right is not available unless expressly conferred by the articles. In the absence of any express provision to this effect, preference shares rank, on winding up, equally with other classes in the matter of repayment of capital.

3. **Participation in surplus profits and assets.** *Sometimes*, especially in the case of companies working a rather speculative class of enterprise, preference shareholders, after receiving the full dividend to which they are preferentially entitled, have also the right to a further share in profits after the ordinary shareholders have received a certain amount of dividend. A preference share having such a right is called a cumulative participating preference share. Such a share is very strongly protected. It carries the right to a fixed dividend before the ordinary shareholders receive anything, so that if the company is only moderately successful, its service has to be considered first, and at the same time if the company earns big profits it gets some share in them after the ordinary shareholders have had their slice. This form of preference share is not, however, common. Preference shares are, however, entitled to their proportionate share of any surplus assets on winding-up, after arrears of dividend, if any, have been met and all capital repaid, unless that right has been expressly or by clear implication taken away. This is the legal position; but in practice companies usually issue preference shares subject to a provision which entitles them, on winding up, to priority as to repayment of capital and arrears of dividends up to the commencement of winding up over other classes, but no further right to participate in profits or assets.

The following extracts from published prospectuses are specimens illustrating the participating rights attached to preference shares :—

'The dividend of Rs. 6 per cent. per annum on the preference shares is cumulative and the preference shares are preferential as to capital as well as dividend. In the event of a dividend of 10 per cent. or over being declared on ordinary shares, the preference shares will be entitled to dividend at 7 per cent. per annum during such year and will, subject to a maximum of Rs. 9 per cent per annum, be entitled to an additional Re. 1 per cent. dividend for every additional 10 per cent. of dividend on ordinary shares." *Amrit Banaspati* Co., *Ltd.* In this case the preference shares are entitled to their proportionate share of any surplus assets on winding-up, because that right has not been expressly taken away.

"The cumulative preference shares are entitled to a cumulative preferential dividend at the rate of 6½% per annum (free of income-tax) and to rank, both as regards dividend and capital, in priority to the ordinary shares in the event of a winding up and are entitled to further participation in profits and other special rights as follows :—

(a) That if in any year a dividend of 10% is paid to the ordinary shareholders, the preference shareholders will be entitled to half per cent. more, *i. e.*, 7% per annum free of

income-tax. Thereafter for every extra one per cent, over aod above ten per cent. paid on ordinary shares, these preference sbares shall be entitled to a quarter per cent. more.

(b) In all other respects, these cnmnlative preference shares confer the same rigbts and privileges and carry with them the same obligations as are provided for the ordinary shares in the articles and memorandnm of association." *The Nellore Power & Light, Ltd.*

"The preference shares are, in the first instance, entitled to a cnmulative dividend of 6 per cent. free of tax. Thereafter dividend np to 16 per cent free of tax is payable on ordinary sbares. Such portion of the balance, if any, as is available for dividend after the aforesaid declaration is distributable as to one-fourth to preference shares and three-fourths to nrdinary shares." *India Collective Farms, Ltd.*,

"The Cumnlative Preference Shares shall confer the right to a fixed cumnlative preferential dividend at the rate of 5 per cent. per annum without deduction of iocome-tax on the capital for the time being paid up thereon, and the right in a winding up to payment of capital and arrears of dividend, whether declared or earned or not, up to the commencement of the winding np, in priority to the Ordinary Shares, bot shall not confer any further right to participate in profits or assets." *Steel Corporation of Bengal, Ltd.*

4. *Rights at General Meetings.* The rights of preference shares with regard to the receipt of notice of, and to attend and voting at, the general meetings of the company are governed by the articles. Preference shares may have equal voting powers with ordinary shares, bot it is usual to restrict the preference share voting power, and frequently to withhold voting right until the dividend is in arrear. Tbe following are some of the specimen provisions with regard to the right to vote, attend and speak at general meetings of companies :—

'The articles of association do not confer tbe right to attend or vote at general meetings of the Corporatinn on the holders of preference shares nnless the dividend nn sncb shares is in arrear for one year. Subject to aforesaid, nn a show of hands every member present in person and entitled to vote shall have one vote, and on a poll every member present in person nr by proxy shall have one vote for every share held by him No member may vote, act as proxy, or be reckoned in a quorum whilst any call or nther sum shall be due and payable to tbe Corporation in respect nf any nf the shares of such member." *Steel Corporation of Bengal, Ltd.*

"The holders of preference shares shall not be entitled to any voting rights, but may be entitled to be present at any meeting of the Company with the permission nf the Chairman. Preference shares confer the right to receive nntice of or vote at general meetings only when the dividend on such shares is in arrear for twelve calendar months or when any resolntion is proposed for reducing the capital of the Company or for winding up the Company or directly affecting the interest of bolders of snch sbares as a class as regards dividend,

retnrn of capital or voting. Upon any qnestion which entitles the holders of preference shares tn vote, these shares shall confer one vote for each share held." *Amrit Banaspati Co., Ltd.*

5. **Right to appoint directors.** Occasionally, in order to make preference share more attractive to investors, it is provided that the preference shareholders shall have the right to appoint one or more directors of the company. In the case of the Nellore Power & Light, Ltd., one seat on the hoard of directors has heen reserved for the preference shareholders.

6. **Restriction on Creation of Prior Rights.** A company which has already issued preference shares may make a fotnre issue of capital having priority over the existing preference shares. The new shares will then be known as 'pre-preference shares'. Unless the preference shareholders' rights are properly safeguarded in this respect by a suitable provision in the company's memorandom or articles, the company may create shares having prior claims to dividends and capital without consnlting the existing preference shareholders whose interests are prejudiced. An example of a desirable protective clanse, taken from the Prospectus of Nellore Power and Light, Ltd., is reprodnced helow :—

"Nn more shares ranking on an eqnal footing with the present issue of preference shares shall be issued by the Company without the previous consent of three-fourths majority of the said preference shareholders."

7. **Right of Conversion.** Where a right of conversion is attached to preference shares, the preference shareholders can convert them into another class of shares, e. g., ordinary or deferred, within a specified time. The right of conversion is nsnally attached to redeemahle preference shares. The prospectus of Olympia (Calcutta), Ltd., dated 27th May, 1938, which offered to the public 500 6 per cent. cnmnlative redeemahle preference shares of Rs. 100 each and 36,500 ordinary shares of Rs. 10 each, stated, *inter alia*, that "the holders of the preference shares shall have the option, while they remain nnredeemed, of converting the preference shares into ordinary shares on the hasis of ten ordinary shares for every preference share."

Where preference shares have the right of conversion, they are called convertible preference shares.

8 **Rights to take Ordinary Shares.** By the prospectns of the Alkali & Chemical Corporation of India, Ltd., dated 21st Febroary, 1938. 31,000 preference Shares of Rs. 100 each were offered to the public at par with the following rights :—

Each preference Share allotted shall carry with it the option of taking np 6 Ordinary Shares of Rs. 10 each at par. The terms upon which snch option is exercisahle are as follows :—

(1) The option may he exercised by the registered holder serving on the Company at its registered office a written notice of his intention to exercise the nption. The full amount payable in respect of the shares shonld accompany the notice,

and no allotment will be made nntil payment in full is received.' If payment in fnll is not received withen ten days of the receipt of the notice, the notice will be rendered inoperative.

(2) The shares allotted in respect of the exercise of any such option will not share in any dividend declared in respect of the financial year of the Company during which the option is exercised.

(3) The option may not be exercised before the 1st day of Jannary 1941, nor after the 30th day of June, 1941.

(4) Only the registered holder for the time being of any Preference Share will be recognised hy the Company as having any right to exercise the option in respect of such share. The certificate relating to the Preference Share in respect of which the option is exercised should be sent to the Registered Office of the Company with the notice of the exercise of the option and no allotment of sbares In pursuance of the option will be made until the Certificate is received.

(5) The option attached to any Preference Shares may only be exercised in full and snbscriptions for less than the full nnmber of 6 Ordinary Shares will not be permissible.

9. **Guarantee Right.** Preference shares issued by a company may be guaranteed as to dividend and repayment of capital by another company. Gnaranteed preference shares offer to the investor additional security. The 30,000 6 per cent. (tax-Iree) cumulative first preference shares of Rs. 100 each issned by the Dunlop Rnbber Co. (India), Ltd., are nnconditionally guaranteed both as regards capitsl and dividend by the Dunlop Rnbber Co , Ltd., of England.

The Imperial Chemical Indnstries (India), Ltd., has entered into an agreement with the Company (The Alkali & Chemical Corporation of India, Ltd ) whereby for a period of five years from the 1st day of April 1938, in any half-year in whicb the Company does not make a distribution of the fixed comulative dividend of 5 per cent, or to the extent to which it does not do so, Imperial Chemical Industries India), Ltd , undertakes to pay to Trustees for distribution to each Preference Shareholder such an amount, as with the distribution (if any) made by the Company, will amount to 5 per cent. per annum on the capital for the time being paid up on the Preference Shares held by him. In addition, Imperial Chemical Industries (India), Ltd., will pay the sum necessary to discharge the liability to Indian Income-Tax on any sum paid under the guarantee.

*10 Redemption Rights.* A company issuing preference shares may undertake to redeem them after a specified period or after giving a specified period's notice. Such preference shares are called redeemable preference shares. Redeemable preference shares may very appropriately be issued by a company in the following circums'ances:- (*a*) When semi-permanent finance is to be raised, preference shares may be issued with an option for the company to redeem them after a specified period; (*b*) Wben, in times of high interest rates, the long view suggests a lower rate, the issue of redeemable preference shares is very appropriate, because full advantage can be taken of subsequent conversion to lower rates; and (*c*) When

a company capitalises its profits, the bonus shares can very properly be issued in the form of redeemable preference shares, so that, if necessary, they may be redeemed out of future profits.

It is, however, possible to a certain extent that the power to issue redeemable preference shares may unfavourably react against the raising of preference share capital, as shares which the company has power to redeem in the event of money rates falling would not commend themselves to every investor. But in order to compensate the preference shareholders for their possible loss of income on redemption and provide an additional inducement to invest in the issue, such shares may be redeemable at a premium, or there may be attached to an issue of redeemable preference shares an option for the holders to take up at par or at a fixed premium shares of another class. In the event of the initial capital expenditure becoming fully productive by the redemption date, the right of conversion may be of considerable value and would more than compensate the holders for a possible loss of income on redemption.

On the other hand, it must not be overlooked that redeemable preference shareholders possess a reasonable assurance that their capital will be repaid at the price determined at the time of issue, and the risk of depreciation in the value of their shares is accordingly diminished.

The issue of redeemable preference shares has been authorised for the first time by section 105-B of the Indian Companies Act, 1913, which was inserted by the Indian Companies (Amendment) Act of 1936, which came into force on 15th January 1937. A company issuing redeemable preference shares may provide for their repayment only by creating a "Redemption Reserve Fund" out of profits, which would otherwise have been available for dividends. The following extract taken from the prospectus of Olympia (Calcutta), Ltd., dated 27th May 1938, is a specimen provision regarding the issue of redeemable preference shares:—

"The preference shares are redeemable at the option of the Directors on a date not later than five years from the commencement of business of the Company to be fixed by three months' previous notice in writing to be served on each holder of the preference shares in the manner in which notices are hereinafter required to be served on members and for the purpose of such redemption the Directors shall in the meantime transfer every year after paying the preferential dividend of 6 per cent, on the amount for the time being paid up on the said preference shares a sum not being less than Rs. 9,000 out of the balance of the profits available for dividend on ordinary shares to a Reserve Fund to be called 'The Capital Redemption Fund" until the amount of such fund is equal to the amount to be applied in redeeming the shares. The holders of the preference shares shall have the option, while they remain unredeemed, of converting the preference shares into ordinary shares on the basis of ten ordinary shares for every preference share."

### Redemption of Preference Shares.

Under section 105B, a company limited by shares may, if so anthorised by its articles, issue preference shares which are, at the optiou of the company, capable of being redeemed. Particnlars of all redeemable preference shares must be inclnded in every Balauce Sheet of compauy specifying (*a*) what part of the issued capital consists of snch shares and (*b*) the date on or before which the shares are liable to be redeemed, or where no definite date is fixed for redemption, the period of notice to be given for redemption.

The share capital of a limited company forms a fund which, snbject to the incidence of losses, is always available to meet the claims of creditors Therefore, in order to protect the interest of creditors, rigorous restrictions are imposed on the redemption of preference shares. The shares cannot be redeemed unless they are fully paid ; and they can be redeemed only (*a*) out of proceeds of a fresh issue of shares made for the purpose, or (*b*) out of profits otherwise available for dividend, or (*c*) out of sales proceeds of any property of the company. Subject to these restrictious, the redemption may be made on such terms and in such mauner as may be provided by the artleles of the compauy.

**Redemption out of the proceeds of a fresh Issue.** If preference shares are to he redeemed out of the proceeds of a fresh issue of shares, there is no restriction except that any premlum payahle on redemption must he provided out of profits before the redemption.

Where a fresh issne of shares is made to provide the funds for the redemption, such an increase is not to be deemed to be an increase of share capital for the purpose of calculatiug the fees payable on capltal provided the redemption takes place withiu oue month of the issue.

It is obvious that, where the redemption is made out of the proceeds of a fresh issue of shares, there is no reduction of the company's share capital. All that occurs is the carrying out of a simple conversion operation. New shares are issued on snch *terms as the company thinks fit and the state of the market* makes possible, aud these new shares replace the shares which are to be redeemed. At no point iu the operation is the capital reduced by a solitary penny. In fact, during the interval which elapses between the date of the issue of the new shares and the date of the redemption of the old shares, there is necessarily a temporary increase of capital.

**Redemption out of profits or out of sale proceeds of any property.** Where the redemption of preference shares is made out of profits available for dividends or ont of sale proceeds of property, there must be transferred out of such profits to a "Capital Redemption Reserve Fund" a snm equal to the amount applied in effecting the redemption. In the absence of this provision, each redemption of preference shares ont of profits available for dividend or out of sale proceeds of property wonld involve a reduction of share capital.

When preference shares are redeemed in this way, the assets of the company are of course reduced by the sum paid out to the shareholders, but, since such assets represent profits available for dividend and not capital, there is no reduction of share capital in any way.

The provision for the redemption of preference shares out of sale proceeds of any property of the company is found only in our law and not in the English Companies Act from which section 105B has been borrowed The sale proceeds of property simply increase the amount of cash or other assets available, but unless there are sufficient undistributed profits, the preference shares cannot be redeemed. It follows, therefore, that both the methods, i. e., redemption out of profits and redemption out of sale proceeds of property—are essentially the same, because in both cases it is necessary to transfer out of profits available for dividend to a Capital Redemption Reserve Fund a sum equal to the amount applied in redemption.

**Capital Redemption Reserve Fund.** The employment of this fund is rigorously restricted. Not only is it incapable of being used for revenue requirements, but it would also be illegal to utilise any portion of it for normal capital purposes such as writing off share and debenture discounts, goodwill, etc *Jones: Guide to Company Balance Sheets* p 69. This fund cannot be reduced except in accordance with the rules relating to the reduction of share capital as contained in section 55-66. If, however, a fresh issue of shares is made after the creation of a Capital Redemption Reserve Fund, the fund may be used up to the nominal value of the new shares issued, in paying up bonus shares. It is not necessary that the new shares should be fully called; it is sufficient that they be issued so that the company can make the call at any time. The bonus shares can then be issued to the nominal value of the new shares.

**2. Ordinary Shares.**

The ordinary shares are those that rank for dividend and capital repayment after the preference shares, but (unless there are deferred shares) they take the whole of profit remaining for distribution after the fixed preference share dividends have been paid. They give to the owners not only a varying dividend prospect but also the opportunity of capital appreciation on market values

*Preferred Ordinary Shares* The holders of these shares have the right to a non-cumulative fixed dividend after the claims of the preference share-holders have been met and before the ordinary shares rank for dividend. Preferred ordinary shares thus occupy a position between the preference shares and the ordinary shares, or where no preference shares have been issued, they have the same status as preference shares.

**3. Deferred Shares.**

The deferred shares rank for dividend after all the other classes of shares have received fixed rates of dividend. They are generally few in number and small in nominal value, but the voting powers which

they command and the profits to which they are entitled are often considerable. The following extract will illustrate this point:—

The Amrit Banaspati Co., Ltd., issued a prospectus dated 23rd April 1940, by which it issued 20,000 preference shares of Rs. 10 each, 90,000 ordinary shares of Rs 10 each and 90,000 deferred shares of Re. 1 each. Of these 3,500 ordinary shares were allotted to the signatories to the memorandum of association; 36,500 ordinary shares and 40,000 deferred shares were reserved for allotment to the directors and their associates; and the balance was offered to the public for subscription. Every ordinary or deferred share had one vote while the holders of preference shares were disfranchised. The deferred shares will not be eligible for a dividend unless a dividend of 6 per cent. is declared on the ordinary share capital for the time being paid up. If a dividend of 6 per cent., or above is declared on the ordinary shares, holders of the deferred shares will be paid a dividend at the same rate as that paid on the ordinary shares up to 10 per cent. If, after payment of dividends on preference, ordinary and deferred shares, any surplus amount is available out of the profits allocated for distribution, such surplus will, as to one-half, be distributed amongst the ordinary shareholders pro rata on the paid-up capital and, as to the remaining half, amongst the deferred shareholders pro rata on the paid-up capital.

From the above example it is obvious that the deferred share capital is considerably less than the ordinary share capital; and yet, if the company is prosperous, the deferred shareholders become entitled to profits quite disproportionate to the amount of their capital. Thus, if we assume, that the entire issued capital of the Amrit Banaspati Co., Ltd., is fully paid and that in one year, after paying off the preference share dividend, there is a profit of Rs. 2, 79,000 available for distribution amongst the ordinary and deferred shareholders, then the ordinary shareholders get only 20 per cent. whilst the deferred shareholders score a dividend of 110 per cent. This is why the deferred shares are regarded as an ingenious device for keeping for the original promoters or vendors a very substantial share in the profits and at the same time preserving for them an air of great modesty and moderation. In this connection it may be noted that the deferred shares (sometimes also known as founders or management or vendors shares) are usually taken up by the management.

### Classes of Share Capital.

The share capital of a company is the money subscribed by the shareholders for the purposes of the company. and is divided into the following classes:—

**1. Nominal, Registered or Authorised Capital.** This is the amount set out in the memorandum of association which the company has power to issue. An ad valorem duty has to be paid on the original nominal capital of a company and on any subsequent increase thereof irrespective of the amount actually issued. The nominal capital is divided into shares, each of so many rupees.

**2. Issued or Subscribed Capital.** This is the capital consisting of the number of shares that have been actually allotted by the company to the shareholders, i. e., issued by the company and subscribed for by

the shareholders. So long as the number of shares allotted by the company continue to be held by the shareholders, the terms issned and snbscribed capitals are ,the same. But if some of the shares once allotted by the company are subseqnently forfeited for non-payment of calls, a distinction is made by some companies between the term issued capital and the term snbscribed capital. The term issued capital in such circumstances is used for the total number of shares allotted by the company ; while the term subscribed capital stands for the actual nnmber of shares held by the shareholders, i. e., the nnmber of shares allotted minns the nnmber of shares forfeited.

3. **Called up Capital** This is the amount of money called np on the shares actually issued. A company does not necessarily require the fnll amount of the sbares at once, and therefore it calls up only snch amount as it needs.

4. **Paid up Capital.** This is the amount of the called np capital which has actnally been paid by the shareholders to the company. The paid-up capital will be less than the called-up capital, if some of the shareholders fail to pay the call made upon their shares. The difference between the called-up capital and the paid-up capital is known as *calls in arrear*.

Some companies nse the term issned capital for the number of shares which they offer to the pnblic by means of the prospectns whether that has been allotted or not. Legally speaking snch invited capital is not and cannot be called issued capital.

**Requirements of Form F with regard to Share Capital-** According to Form F, the following information relating to the share capital is to be disclosed in the balance sheet of a company :—

Capital :—

Authorised Capital.......... shares of Rs... ......each.

(Distinguishing between the various classes of capital)

Issued Capital.........shares of Rs. . .......each

(i) Shares issned as fnlly paid up pursuant to any contract without payments being received in cash ...........shares of Rs .......... each.

(ii) Shares issued for payments in cash.................. ..shares of Rs......... ...each.

Subscribed Capital..... ......shares of Rs..............each

Amount called np at Rs. . .........per share

**Less** Calls nnpaid......

(i) Due from Managing Agents

(ii) Due from others

**Add** Forfeited Shares (amount paid up)

Note —Where circumstances permit, issued and subscribed capital and amount called np may be shown as one item e. g.,

Issned and Subscribed Capital............shares of Rs..........— each, Rs............called up

The above-mentioned requirements of law may now be summarised as follows:—

1. The authorised, issued, subscribed, called-up and paid up share capitals are to be shown separately together with the different classes of shares under each head. The authorised capital may, however, include a number of shares that have not been classified such shares to be classified only when they are actually issued.

2. With regard to the issued capital a distinction is to be drawn between *(a)* shares issued as fully paid up pursuant to any contract without payments being received in cash, e. g., shares allotted as fully paid to promoters and vendors or allotted as bonus shares, and *(b)* shares issued for payments in cash. Some companies whose shares are presumably issued for cash do not state this fact under the heading of issued capital leaving *it only* implied; but it is better to make this fact clear on the balance sheet.

3. The unpaid calls are to be shown as a deduction from the called-up capital, the calls due from managing agents and those due from others being stated separately. There is no express provision that calls due from directors should also be mentioned separately. But it is thought that calls due from directors are a debt due from them to the company under the provisions of section 21 (2), and, since all debts due from directors are to be stated as a separate item on the balance sheet, *it is* necessary that the calls due from directors should also be given separately.

4. If there are any redeemable preference shares, section 105-B requires that the following particulars relating to them should be disclosed: *(a)* their amount, and *(b)* the date of their redemption, or, where no such date is fixed, the period of notice to be given for their redemption.

5. Where circumstances permit, the various classes of share capital may be shown as one item.

6. The amount received on forfeited shares is to be shown as an addition to the paid-up capital; but good accounting requires that it should not be coupled with paid-up capital, because it is not a part of the dividend-bearing capital of the company.

7. Any other capital receipts such as the following, if not credited to capital reserve, are to be stated separately after paid up capital: *(a)* Calls received in advance; *(b)* Premium realised on the sale of shares; *(c)* Amount received on remission of forfeiture; *(d)* Amount received from sale of shares on which the company's lien is enforced, and *(e)* Any balance remaining in the reduction of capital account.

8. Bonus shares pending allotment on the date of the balance sheet may be shown separately from paid up capital under the heading "Capital Fund Account" or "Capital in Suspense".

9. Monies received in respect of shares which have not been allotted on the date of the balance sheet should not be shown as capital, but they should appear as a separate item as "New Issue

Application Deposit" or "Amount Received on Shares Pending Allotment".

10. If on the date of the balance sheet, there are any outstanding share coupons in respect of fractional shares allotted by the company, a note in respect of them should be made in connection with the share capital.

These points are now to be illustrated by extracts from the actual published balance sheets of Indian companies.

## SHARE CAPITAL

1. The Dunlop Rubber Co. (India) Ltd.,—B/S on 31st December 1940.

| | Authorised Rs | Issued and Subscribed Rs. |
|---|---|---|
| Share Capital :— | | |
| 30,000 6% (Tax-free) Guranteed Cumulative Preference Shares of Rs. 100 each, fully paid | 30,00,000 | 30,00,000 |
| 40,000 6% Second Cumulative Preference Shares of Rs. 100 each, fully paid | 40,00,000 | 40,00,000 |
| 5,00,000 Ordinary Shares of Rs. 10 each, fully paid of which | | |
| (a) 1,99,900 Shares issued as fully paid up otherwise than in cash | 19,99,000 | 19,99,000 |
| (b) 3,00,100 Shares issued for payment wholly in cash | 30 01,000 | 30,01,000 |
| 8,00,000 Shares of Rs. 10 each (non-categorised) | 80,00,000 | |
| | 2,00,00,000 | 1,20,00,000 |

2. The Elgin Mills Co., Ltd.,—B/S. on 30th September 1940.

| | Rs. | Rs. |
|---|---|---|
| Capital :— | | |
| Authorised, Issued and Subscribed :— | | |
| 11,000 8% Cumulative Preference Shares of Rs. 100 each fully paid up in cash | 11,00,000 | |
| 1,60,000 Ordinary Shares of Rs. 10 each fully paid up in cash | 16,00,000 | |
| 50,000 Vendors Shares of Rs. 10 each fully paid up otherwise than in cash | 5,00,000 | 32,00,000 |

3. **The Delhi Cloth and General Mills Co. Ltd.,—B/S. on 30th June 1940**

| | Rs | Rs. |
|---|---|---|
| Share Capital : | | |
| **Authorised:** | | |
| 5,15,000 Ordinary shares of Rs. 25 each | 1,28,75,000 | |
| 50,000 Ordinary Shares of Rs. 2/8/- each | 1,25,000 | |
| 80,000 4½% Cumulative Preference Shares of Rs 25 each | 20,00,000 | |
| | 1,50,00,000 | |
| **Issued and Subscribed.** | | |
| *(i)* Shares issued for payment in cash :— | | |
| 40,000 Ordinary Shares of Rs. 25 each | 10,00,000 | |
| 5,333 Ordinary Shares of Rs. 25 each | 1,33,325 | |
| *(ii)* Shares issued as fully paid up without payment being received in cash:— | | |
| 40,000 4½% 1st Cumulative Preference Shares of Rs. 25 each (issued as Bonus Shares vide Shareholders' Resolution dated 16-9 1931) ... | 10,00,000 | |
| 40,000 4½% 2nd Cumulative Preference Shares of Rs. 25 each (issued as Bonus Shares vide Shareholders' Resolution dated 31-10-1935) ... | 10,00,000 | |
| 4,49,330 Ordinary Shares of Rs 25 each (issued as Bonus Shares vide Shareholders' Resolution dated 11-3-1939) ... | 1,12,33,250 | |
| 40,000 Ordinary Shares of Rs. 2/8/- each (issued as Bonus Shares vide Shareholders' Resolution dated 11-3-1939) ... | 1,00,000 | |
| | 1,44,66,575 | |
| **Called-up** | | |
| 4,89,198 Ordinary Shares of Rs. 25 each, fully paid ... | 1,22,29,950 | |
| 5,333 Ordinary Shares of Rs. 25 each, Rs 12/8/- paid ... | 66,662-8 | |
| 40,000 Ordinary Shares of Rs. 2/8/ each, fully paid ... | 1,00,000 | |
| 40,000 4½% 1st Cum. Pref. Shares of Rs. 25 each, fully paid ... | 10,00,000 | |
| 40,000 4½% 2nd Cum Pref Shares of Rs. 25 each, fully paid ... | 10,00,000 | |
| | 1,43,96,612 8 | |
| *Less* Calls in arrears ... | 30 0 | 1,43,96,582-8 |
| Calls paid in advance | | 66,362-8 |
| Capitalisation Fund Account | | |
| Balance as per last Balance Sheet | 7,400 | |
| *Less* Transferred to Capital being Bonus Shares issued during the year | 4,100 | 3,300 |

**4. The Finlay Mills, Ltd. B/S. on 31st December, 1940**

| | Rs. | Rs. |
|---|---|---|
| Capital :— | | |
| Authorised :— | | |
| 40,000 Shares of Rs. 100 each ... | 40,00,000 | |
| Issued and Subscribed-— | | |
| 40,000 Shares of Rs 100 each fully paid up (issued as 8,000 Shares of Rs 250 each for payment in cash, subsequently increased and converted into 40,000 Shares of Rs. 100 each from the capitalisation of undivided profits) | | 40 00 000 |

**5. The Saran Engineering Co , Ltd.—B/S. on 31st March 1940**

| | Rs. | Rs |
|---|---|---|
| Capital— | | |
| Authorised·— | | |
| 5,00,000 Shares of Rs. 2 each ... | | 10,00,000 |
| Issued and Subscribed— | | |
| 1,00,000 Shares of Rs. 2 each fully paid up in cash . | 2,00,000 | |
| 50,000 Shares of Rs. 2 each issued as Special Capital Bonus ... | 1,00,000 | 3,00,000 |

**6. Smith, Stainstreet & Co., Ltd —B/S. on 30th June 1940**

| | Rs | Rs. |
|---|---|---|
| Capital :— | | |
| Authorised :— | | |
| 10,000 10% Preference Shares of Rs. 50 each fully paid, Cumulative as to 7% and non-cumulative as to the remaining 3% (Reduced from 7% Cumulative Preference Shares of Rs. 100 each fully paid by a Court Order dated 7th June 1937 ... | 5,00,000 | |
| 1,00,000 Ordinary Shares of As. -/4/- each fully paid (Reduced from Rs 10 each fully paid to Rs. 2/8/- by a Court Order dated 31st August 1931 and further reduced to As -/4/- each by a Court Order dated 7th June 1937) ... | 25,000 | |
| | 5,25,000 | |
| Issued and Subscribed :— | | |
| Shares issued for payment in cash :— | | |
| 10,000 10% Preference Shares (Cumulative as to 7% and non-cumulative as to the remaining 3% of Rs. 50 each fully paid ... | 5,00,000 | |
| Shares issued as fully paid up pursuant to a contract without payment being received in cash :— | | |
| 1,00,000 Ordinary Shares of As. -/4/- each | 25,000 | 5,25,000 |

7. **The Bombay Dyelng & Mfg Co., Ltd. – B/S. on 31st December 1940**

| | Rs. | Rs. |
|---|---|---|
| Capital :— | | |
| **Authorlsed :—** | | |
| 25,600 Ordinary Shares of Rs. 250 each | 62,00,000 | |
| **Issued and subscribed :—** | | |
| 25,098 Shares of Rs. 250/- each fully paid up | | 62,74,500 |

*Note.*—Apparently the 25,098 Shares were issoed for payment in cash, but this fact is not stated.

8. **The Titaghur Paper Mills Co., Ltd.—B/S, on 31st March 1941**

| | Rs. | Rs. |
|---|---|---|
| Capital— | | |
| **Authorlsed :—** | | |
| 11,500 8% First Cumulative Preference Shares of Rs 100 each ... | 11,50,000 | |
| 15,000 5% Second Cumulative Preference Shares of Rs. 100 each, redeemable on or after 30th September 1946 at a premium of Rs. 5 ... | 15,00,000 | |
| 1,75,000 Preferred Ordinary Shares of Rs. 2-8-0 each fully paid up ... | 4,37,500 | |
| 3,50,000 'A' Ordinary Shares of Rs. 5 each | 17,50,000 | |
| 3,50,300 'B' Ordinary Shares of Rs. 5 each | 17,51,500 | |
| | 65,89,000 | |
| **Issued and Subscribed :** | | |
| For Cash— | | |
| 11,500 8°/。 First Cumolative Preference Shares of Rs 100 each fully paid op ... | 11 50,000 | |
| 15,000 5°/。 Secood Cumulative Preference Shares of Rs. 100 each, fully paid up, redeemable oo or after 30th September 1946 at a premiom of Rs. 5 ... | 15,00,000 | |
| 1,75,000 Preferred Ordinary Shares of Rs 2-8-0 each, fully paid up ... | 4,37,500 | |
| **For consideration other than Cash—** | | |
| 3,50,000 "A" Ordinary Shares of Rs. 5 each, fully paid | 17,50,000 | |
| 2,86 609 "B" Ordinary Shares of Rs. 5 each fully paid 14,33,045 | | |
| **For Cash—** | | |
| 63,691 "B" Ordinary Shares of Rs. 5 each fully paid 3,18,455 | | |
| | 17,51,500 | |
| | | 65,89,000 |

*Note*—This can be better shown as follows :—

| | Rs | Rs. |
|---|---|---|
| Capital—Authorised, Issued and Subscribed— | | |
| 11,500 8% First Cumulative Preference Shares of Rs. 100 each, fully paid up in cash | 11,50,000 | |
| 15,000 5% Second Cumulative Preference Shares of Rs 100 each (redeemable on or after 30th September 1946 at a premium of Rs 5) fully paid up in cash .. | 15,00,000 | |
| 1,75,000 Preferred Ordinary Shares of Rs. 2-8-0 each, fully paid up in cash . | 4,37,500 | |
| 3,50,000 "A" Ordinary Shares of Rs. 5 each fully paid up in cash ... | 17,50,000 | |
| 3,50,300 "B" Ordinary Shares of Rs. 5 each. fully paid up (of which 63,691 shares issued for cash and 2,86,609 shares issued for consideration other than cash) ... | 17,51,500 | 65,89,000 |

**9. The Assam Saw Mills & Timber Co., Ltd.,—B/S. on 30th September 1940**

| | Rs | Rs. |
|---|---|---|
| Capital :— | | |
| Authorised Capital :— | | |
| 10,20,000 Ordinary Shares of Re. 1 each | 10,20 000 | |
| Issued and Subscribed Capital :— | | |
| I—Shares issued as fully paid up pursuant to an agreement of 11-3-18 without payment being received in cash—20,000 Ordinary Shares of Rs. 10 each ... | 2,00,000 | |
| II—Shares issued for payment in cash—1,20,000 Ordinary Shares of Rs. 10 each ... | 12,00,000 | |
| | 14,00,000 | |
| *Less*—Capital reduced on 20-3-24 from Rs 10 per share to Rs. 3 per share | 9,80,000 | |
| | 4,20,000 | |
| III—Shares issued as fully paid up pursuant to an agreement of 18-7-24 otherwise than in cash—1,50,000 Ordinary Shares of Rs. 3 each | 4,50,000 | |
| IV—Shares issued for payment in cash—5,052 Ordinary Shares of Rs. 3 each | 15,156 | |
| | 8,85,156 | |
| *Less*—Capital reduced on 27-7-39 from Rs. 3 per share to. Re. 1 per share | 5,90,104 | 2,95,052 |

10. The Tata Oil Mills Co., Ltd.—B/S. on 31st March 1941

| | Rs | Rs. |
|---|---|---|
| Capital :— | | |
| Authorised Capital .— | | |
| 3,00,000 Ordinary Shares of Rs. 25 each | 75,00,000 | |
| Issued Capital :— | | |
| (1) Shares issued as fully paid up without payment being received in cash pursuant to clause 4 of the Scheme of Arrangement of July 1928 :— | | |
| 88,000 Shares originally issued as 6°/₀ Non-cumulative Preference Shares of Rs. 25 each but converted into Ordinary Shares of the same value by a Special Resolution passed at the Extra Ordinary General Meeting held on 21-4-1938 | 22,00,000 | |
| (2) Shares issued for payment in cash :— | | |
| 95,158 Ordinary Shares of Rs. 25 each 23,78,950 | | |
| 40,765 Ordinary Shares of Rs.25 each issued during this year 10,19,125 | 33,98,075 | |
| 2,23,923 | 55,98,075 | |
| Subscribed Capital:— | | |
| 88,000 Ordinary Shares of Rs. 25 each converted from 6°/₀ Non cumulative Preference Shares of the same value as stated above | 22,00,000 | |
| 91,741 Ordinary Shares (including 25 shares forfeiture of which was remitted during this year) of Rs. 25 each ... | 22,93,525 | |
| 40,765 Ordinary Shares of Rs. 25 each issued during the year on which Rs.15 per share has been called up 6,11,475 | | |
| *Less* Allotment money at Rs 5 per share on 138 shares (since paid) ... 690 | 6,10,785 | |
| 3,417 Ordinary Shares forfeited so far | | 51,04,310 |
| 2,23,923 | | |

**11. The Indian Iron and Steel Co., Ltd. B/S. on 31st March 1940**

| *31-3 1939 £ | 31-3 1940 £ | Capital— | 31-3 1940 | 31-3 1939 |
|---|---|---|---|---|
| | | **Authorised Capital—** | Rs. | Rs. |
| 3,750,000 | 3,750,000 | 50,00,000 Shares of Rs 10 each 5,00,00,000 | | |
| | | **Issued and Subscribed Capital—** | | |
| | | 15,16,590 Ordinary Shares of Rs. 10 each fully paid in cash | 1,51,65,900 | |
| | | 7,14,462 Ordinary Shares of Rs. 10 each fully paid for a consideration other than cash | 71,44,620 | |
| | | 4°/₀ Convertible Second Mortgage Debenture Stock converted in accordance with the Prospectus dated 2nd December 1936, and allotted Ordinary Shares as fully paid for a consideration other than cash— Converted to 31 3-1939 £ 456,990 and shares allotted 3,04,660 Ordinary Shares of Rs. 10 each 30,46 600 Converted from 1-4-1939 to 31-3-1940 £ 2,814 and shares allotted 1,876 Ordinary Shares of Rs 10 each 18,760 | 30,65,363 | |
| 1,901,784 | 1,903,191 | | 2,53,75,880 | 2,53,57,120 |
| | | *Note*—26,797 Ordinary Shares of Rs 10 each have been set aside for issue to the Holders of £ 40,196 4°/₀ C S M D. Stock in the event of the option to convert before 31.12 1943 being exercised. | | |

Eqnivlent sterling value on an exchange basis of 1 s. 6 d. per rupee.

**12. The Ahmedabad Electricity Co., Ltd —B/S. on 30th September 1940**

| | Rs. | Rs. |
|---|---|---|
| Capital— | | |
| Authorised— | | |
| 1,50,000 Ordinary Shares of Rs. 100 each | 1,50,00,000 | |
| Issued— | | |
| 1,00,000 Shares Rs. 100 each ... | 1,00,00,000 | |
| Subscribed and Called up— | | |
| 72,624 Shares of Rs. 100 each, issued for cash and fully paid ... | 72,62,400 | |
| 2,375 Shares of Rs 100 each, issued to promoters as fully paid ... | 2,37,500 | |
| 24,973 Shares of Rs. 100 each, issued for cash and called up at Rs. 50 per share ... | 12,48,650 | |
| 99,972 | 87,48,550 | |
| *Less* Calls in arrears | 9,625 | |
| | | 87,38,925 |
| Forfeited Shares Account— | | |
| 1 Share of Rs 100 fully called up, Rs. 50 paid | | 50 |
| New Issue Application Deposit— | | |
| Received on account of Application and Allotment monies against 6 shares pending allotment ... | | 300 |

**13. The United Mills, Ltd B/S. on 31st December 1943**

| | Rs. | Rs. |
|---|---|---|
| Capital— | | |
| Authorised, Issued and Subscribed: | | |
| 20,00,000 Ordinary Shares of Rs. 10 each converted under Reduction Scheme of 1929 from 20,00,000 Cumulative Preference Shares of Rs. 10 each, which had been issued to vendors as fully paid up ... | 2,00,00,000 | |
| 40,00,000 Deferred Shares of Re. 1 each fully paid up converted under Reduction Scheme of 1929 from 40,00,000 Ordinary Shares of Rs 10 each, fully paid up in cash . | 40,00,000 | |
| 10,00,000 Deferred Shares of Re. 1 each issued under Reduction Scheme of 1929 as fully paid up in lieu of arrears of Cumulative Preference Share Dividends ... | 10,00,000 | 2,50,00,000 |

**14. The Palai Central Bank, Ltd. B/S. on 31st December 1943**

| | Rs | a | p | Rs. | a. | p. |
|---|---|---|---|---|---|---|
| Capital :— | | | | | | |
| Authorised :— | | | | | | |
| 1,60,000 Shares of Rs. 25 each | 40,00,000 | – | – | | | |
| Issued and Subscribed :— | | | | | | |
| 40,000 Shares of Rs 25 each | 10,00,000 | – | – | | | |
| Paid up :— | | | | | | |
| 90 Shares at Rs. 5 each | 450 | – | – | | | |
| 102 „ „ Rs. 10 „ | 1,020 | – | – | | | |
| 27,763 „ „ Rs. 15 „ | 4,16,445 | – | – | | | |
| 2,534 „ „ Rs. 20 „ | 50,680 | – | – | | | |
| 9,511 „ „ Rs. 25 „ | 2,37,775 | – | – | | | |
| 40,000 | 7,06,370 | – | – | | | |
| *Add*—Share Suspense Account | 534 | 7 | 10 | 7,06,904 | 7 | 10 |

*Note.*—It is not clear what the item "Share Suspense Account" stands for. It may represent the amount received on shares forfeited and re-issued. Whatever it is, it should not be coupled with paid up capital.

**15. The Orient Paper Mills, Ltd, B/S. on 31st March 1942**

| | Rs. | Rs. |
|---|---|---|
| Authorised Capital :— | | |
| 5,00,000 Ordinary Shares of Rs. 10 each | 50,00,000 | |
| 50,000 $5\frac{1}{2}$% Cumulative Preference Shares of Rs. 100 each ... | 50,00,000 | |
| | 1,00,00,000 | |
| Issued, Subscribed and Paid up Capital :— | | |
| 2,09,450 Ordinary Shares of Rs. 10 each fully paid ... | 20,94,500 | |
| 20,000 $5\frac{1}{2}$% Cumulative Preference Shares of Rs. 100 each fully paid ... | 20,00,000 | 40,94,500 |
| *Note.*—The Cumulative Preference Shares may be reduced by the Company at its option, either in whole or in part and from time to time, at par (on three months' previous notice) on or after the expiry of 10 years from 25th July 1936, the date of incorporation of the Company (*Vide* Article No 43 (b) of the Company's Articles of Association). | | |
| Forfeited Shares ... | | 3,000 |

**16.** **The Nath Bank, Ltd., B/S. on 31st December 1943**

| | Rs. | a | p | Rs. | a. | p. |
|---|---|---|---|---|---|---|
| **Authorised Capital—** 2,00,000 Shares of Rs. 25 each ... | 50,00,000 | - | - | | | |
| **Issued Capital—** 1,60,000 Shares of Rs. 25 each ... | 40,00,000 | - | - | | | |
| ***Subscribed, Called-up and Paid up Capital*** | | | | | | |
| 86,075 Shares of Rs. 25 each called in full ... | 21,51,875 | - | - | | | |
| 2,394 Shares of Rs 25 each called at Rs. 9-6 per share .. | 22,443 | 12 | - | | | |
| 15,270 Shares of Rs. 25 each called at Rs. 6-4-0 per share ... | 95,437 | 8 | - | | | |
| | 22,69,756 | 4 | - | | | |
| *Less* Calls-in-arrears ... | 4,51,925 | 9 | 11 | | | |
| | 18,17,830 | 10 | 1 | | | |
| *Add* Calls in-advance .. | 2,02 901 | 14 | 8 | 20,20,732 | 8 | 9 |
| Share money in Deposit ... | | | | 593 | 1 | - |

*Notes*—1. The term issued capital in this case is apparently used for the number of shares offered to the public for subscription.

2. Presumably all the shares issued were for payments in cash.
3. *Notice the odd amounts called up per share and also the huge amounts of calls in arrears and calls in advance.*
3. The amounts of calls in advance should not have been added to the paid-up capital.
4. The item "Share money in Deposit" stands for the deposits received in respect of shares which have not yet been allotted.

**17.** **The Apollo Mills, Ltd., B/S on 31st December 1943.**

| | Rs. | Rs. |
|---|---|---|
| Capital :— **Authorised, Issued and Subscribed : ..** | | |
| 50,000 Shares of Rs. 2 each fully paid up converted under Resolution Scheme of 1939 *from 50,000 Shares of Rs 50 each fully paid up in cash* .. | 1,00,000 | |
| 24,50,000 Shares of Rs. 2 each issued as fully paid up pursuant to the Reconstruction Scheme without payment being received in cash ... | 49,00,000 | |
| | | 50,00,000 |

*Note.—The disclosure of the Reconstruction* Scheme is voluntarily given. It is not required by law.

**18. The Podar Mills, Ltd., B/S. on 30th September 1943**

| | Rs. | Rs. |
|---|---|---|
| Capital :— | | |
| **Authorised Capital :—** | | |
| 40,000 Ordinary Shares of Rs. 100 each | 40,00,000 | |
| 5,000 4°/₀ (Free of Income-Tax) Cumulative Preference Shares of Rs. 100 each — | 5,00,000 | |
| 5,000 Preference Shares of Rs. 100 each | 5,00,000 | |
| | | 50,00,000 |
| **Issued Capital :—** | | |
| 20,000 Ordinary Shares of Rs. 100 each | 20,00,000 | |
| 2,000 4°/₀ (Free of Income-Tax) Cumulative Preference Shares of Rs. 100 each ... | 3,00,000 | |
| | | 23,00,000 |
| **Subscribed and paid up Capital :—** | | |
| 20,000 Ordinary Shares of Rs. 100 each | 20,00,000 | |
| 3,000* 4°/₀ (Free of Income Tax) Cumulative Preference Shares of Rs 100 each fully paid ... | 3,00,000 | |
| | | 23,00,000 |
| * (of these Fractional Certificates equivalent to 69 shares remain to be presented to the Company so that as at 30-9-43 the Company had issued Preference Share Certificates for 2,931 shares out of 3,000 shares) ... | | |

*Note.*—It is not stated whether the ordinary and preference shares were issued for payment being received in cash or for any other consideration.

## 2. RESERVES.

The creation of reserves is an important feature of company finance. Before settling the amount of profits avalilable for distribution amongst the shareholders, it is essential that adequate provision be made for the depreciation of block and the taxation liability to government; but it is also equally desirable that the full balance remaining thereafter should not be distributed and that a certain portion thereof should be retained in the business for future use.

The profits to be retained in the business are transferred to reserves of various kinds. The creation of reserves is a matter of prudence in much the same way as an individual endeavours to set aside some portion of his income for the purpose of providing against such contingencies as sickness, unemployment, old age, etc. In the case of an individual, such a provision is known as 'saving', but in business it is called a 'reserve'.

**How Created ?** Reserves represent profits earned—either trading profits or special profits. A reserve is created either by a charge to profit and loss account or else by a transfer of some other

surplus which has not been credited to profit and loss account. Thus, where a reserve is set up out of any special and extraneous profits, that fact is usually referred to in the directors' reports, e.g.

1. "A sum of Rs. 2,41,958, representing the difference between the amount recovered from underwriters for the loss of Thoni Mudi factory burnt down last year and its depreciated valuation in the balance sheet, now written off, has been transferred to Fixed Property Reserve Account." *Bombay Burmah Trading Corporation, Ltd.* Directors' Report for the year ended 31st May 1943.

2. "During the year the Company disposed of 7,600 shares out of its holding of 20,000 shares in the Belsund Sugar Co., Ltd., and the profits on the realisation of these shares have been transferred to a special reserve in the balance sheet." *The U. P. Sugar Co., Ltd.*—Directors' Report for the year ended 30th September 1943.

**General Reserves.** A general reserve is created out of profits or other surpluses simply for the purpose of strengthening the financial position of the company or for meeting unknown contingencies. It is not designed to meet any liability contingency or diminution in the value of assets known to exist as at the date of the balance sheet A general reserve may also be called reserve fund or contingency reserve.

**Special Reserves.** A special reserve is set up for some particular purpose such as a known liability, contingency, commitment or diminution in the value of assets. Such a reserve is usually designated by the purpose for which it is built up, but sometimes it is called simply a special reserve. In recommending the transfer of Rs. 2,50,000 to a special reserve, the directors of the Western India Match Co, Ltd., offered the following explanation in their report for the year ended 31st December 1942:—"At the time the Andaman Islands were occupied by the Japanese, the Government War Risk Insurance Scheme for factories was not in force, and consequently the Port Blair Factory falls outside this scheme. The directors have no information as to what is the condition of the factory at Port Blair at the moment, they, therefore, recommend that Rs. 2,50,000 be set aside out of the year's profit as a special reserve in *respect of this Factory.*"

Given below is a list of special reserves that are met with in the published accounts of Indian companies :—

Dividend Equalisation Reserve
Dividend Adjustment Account
Debenture Redemption Fund
Debenture Sinking Fund
Earthquake Insurance Reserve
Charity Reserve
Fire and Accident Insurance Fund
Mill Insurance Fund
Transit Insurance Fund
Workmen's Insurance Fund
Crop Insurance Fund
Block Improvement Reserve
Employees Benefit Reserve
Benefits to Cultivators Reserve
Workpeople's Gratuity Fund
Workpeople's Housing Fund
Labour Bonus Reserve
Labour Welfare Reserve
Workers Relief Fund
Reserve for Furlough Payments
Reserve for Drainage Scheme
Reserve for Housing Scheme
Reserve for Bad Debts
Taxation Reserve

Fixed Property Reserve
Cane Price Stabilisation Fund
Obsolescence Reserve
Machinery Deterioration Reserve
Machinery Improvement Reserve
Repairs and Renewals Reserve
Depreciation Reserve
Investment Depreciation Fund
Mines Development Fund
Staff Provident Fund
Staff Pension Fund
Officers Retiring Fund
Stock Adjustment Account

*Rehabilitation Reserve
*Reconstruction Reserve
*E. P. T. Deposit Reserve
*Special Depreciation Reserve
*War Contingency Reserve
*Stores and Raw Materials Reserve
*Reserve for Fall in Prices
*Reserve for Deferred Repairs
*Reserve for Enemy Debts
*Reserve for Damage to Factory
*Mill Renovation Reserve
*War Risks Factories Contingency Fund

The name of each reserve in the above list indicates the purpose for which it is created. The Reserves marked with an asterisk are those set up in war-time. Whenever any new special reserve is created, its purpose is usually explained in the directors' report, so that the shareholders may have sufficient knowledge of it. Here are a few extracts in this connection :—

1. "In view of the fact that production is being maintained on an Intensified scale for war purposes, the Board consider that it is prudent, at this stage, to create a Rehabilitation Reserve so that sums thus allocated will be available, when required, against the costs involved, after the present emergency has passed, in recovering the Corporations normal civil trade which meantime has, in most directions, had to be entirely suspended. The amount which it is possible to allocate for this purpose is less than the sum which your directors would have desired to set aside but increased taxation and the maintenance of the usual dividends take up the balance of the amount available for disposal." *The British India Corporation, Ltd.*—Directors' Report for the year ended 31st December 1940.

2. "In view of the increasingly heavy stocks of all descriptions of raw materials and stores at rising prices which the Company is compelled to carry, a further Rs 1,50,000 has been added to the Reserve for Revaluation of Stocks and Stores against the slump in stock values which must be expected" *The Titaghur Paper Mills Co, Ltd* Directors' Report for the half year ended 31st March 1941.

3. "A sum of Rs. 2,00,000 has been set aside in a newly-created Reserve for Deferred Mill Renovations It is considered advisable that this should be done in order that money, which ought to be spent at the present time on capital replacements but which cannot be spent owing to the difficulty of obtaining supplies, should be set aside and accumulated for immediate use when the war is terminated and conditions are normal." *The Titaghur Paper Mills Co., Ltd.*—Directors, Report for the half year ended 30th September 1942.

When the object for which a special reserve is held has been accomplished, it is usually transferred to general reserve, and the fact is indicated for the information of the shareholders in the directors' reports, e. g.

1. 'Your attention is drawn to the fact that the reserves, previously appearing under the headings 'Improvements and Extensions,

'Bamboo Plant', 'Indian Quarters and Welfare Service,' and 'Additional. Qnarters for Apprentices' have been merged into one General Reserve. The objects for which these reserves were created have now been accomplished and transferring them to a General Reserve sets ont more clearly the position of the Company." *The Bengal Peper Mills Co., Ltd*,—Directors' Report for the half year ended 31st December 1940.

2. "As the Reserve for Depreciation on Investments of Rs. 50,000 which appeared in the Balance Sheet as at 30th September 1942, is no longer required, it has been transferred to General Reserve" *The U. P. Sugar Co., Ltd.*—Directors' Report lor the year ended 30th September 1943.

**Capital Reserves** A capital reserve is one which is not available for distribution as dividend. It may be derived from one or more of the following sonrces :—

*(a)* Capital profits which cannot be distributed as dividend such as profit earned prior to incorporation, profit made on the purchase of a business by a company, unrealised appreciation in the value of a fixed asset, premiums received on the issue of shares and debentures, profit on the sale of forfeited shares, or profit on redemption or conversion of debentures if their distribution is repugnant to the company's articles.

*(b)* Any balance remaining in the Capital Reduction Account where the share capital of a company is reduced in accordance with the provisions of section 55.

*(c)* Any general reserve standing in the books of a company whose share capital has been rednced At the fourteenth annnal general meeting of the British India Corporation, Ltd. held in 1934, a shareholder pointed out that in the Company's balance sheet as at 31st December 1932 there was an item of 'General Reserve Rs 20,00,000', while in its balance sheet dated 31st December 1933 there appeared an item called 'Capital Reserve Rs. 20,00,000', and he asked whether there was any difference between these two items. The Chairman of the Company, in reply, said that the term 'General Reserve' which had been used in 1932 had been altered on the suggestion of the Corporation's auditors to 'Capital Reserve', the reason for the alteration being that after the reduction of capital the amount of the reserve could not be utilised lor the payment or equalisation of dividends, and it was deemed advisable accordingly to change the beading to one of 'Capital Reserve.'

*(d)* Profits of an exceptional natnre, which it is desired should not be available for distribution as dividends.

*(e)* Revenue profits which are not represented by liquid assets. The following extract from the Directors' Report of Burrakur Coal Co., Ltd., for the ball year ended 31st December 1940, refers very aptly to this point :—

"Considerable portions of the liquid assets representing General Reserve have been expended in connection with the Loyabad Colliery disaster, and in order to make it clear to shareholders that a portion of the remaining General Reserve is no longer liquid and

therefore no longer available in an emergency, a new account has been opened and designated 'Capital Fund.' The sum of Rs. 30 lakhs has been transferred from General Reserve to this new account, which although in the nature of a fixed capital account still represents reserves built up by the Company. It is evident that fresh liquid reserves will have to be accumulated in order to safeguard the future of the Company."

Sinking Funds A sinking fund is a reserve created out of profits and is usually invested outside the business in easily marketable securities. The object of a sinking fund is to provide a definite capital sum at a definite date for the purpose of repaying a liability or replacing a wasting asset. The word 'sink' in the term sinking fund means to repay, the principal object of a sinking fund being to provide for the repayment of a liability.

When a company issues redeemable debentures or preference shares, the terms of their issue may require it to set up a sinking fund. The cawnpore Textiles, Ltd., issued on 14th May 1938 1,000 4½ per cent. (taxable) Bearer Debenture Bonds of Rs. 250 each, repayable at par on 14th May 1958 with the option of repayment at any time after 14th May 1945, at a premium of 2 per cent, on three months' notice. The Company is required by the terms of this debenture issue to set apart each year out of the profits, for the repayment of the debentures, Rs. 12,500 to form a sinking fund. If in any year the profits do not suffice to provide Rs. 12,500, the deficiency (known as arrears of sinking fund contribution) is to be provided from the profits of the succeeding year or years.

The Central Kurkend Coal Co, Ltd., purchased in 1938 the West Gopalichuck Colliery and in order to meet the cost thereof it increased its authorised capital by the creation of 2,850 6 per cent. (tax free) cumulative redeemable preference shares of Rs. 100 each, of which 2,000 shares were issued at par to the existing shareholders in the proportion of one such share for every 15 shares held and the remaining 850 shares were issued at par to the Gopalichuck Collieries, Ltd., in part satisfaction of the purchase price. These preference shares are redeemable in whole or in part out of the profits of the Company at any time or times at a premium of Rs. 6 per share on one calendar month's notice. By the terms of their issue, the Company is required in each half year to set apart out of the profits Rs. 10,000 to form a sinking fund for the redemption of these shares. If in any half year the profits are insufficient for this purpose, the entire profits which would otherwise have been available for dividends on the ordinary shares shall be transferred to the Capital Redemption Reserve Fund.

A sinking fund grows each year with the aid of periodical contributions and interest. It is built up by setting aside a certain yearly or half-yearly instalment out of profits and by investing it at compound interest outside the business in order to produce a required sum at the end of a given period. If it is assumed that a capital sum of Rs. 1,00,000 will be required in ten years' time to repay a liability and that it will be possible to make investments at 3 per cent. per annum interest, then so much amount must be set aside and invested each year for the next ten years as, at 2 per cent. per annum

compound interest, will produce Rs. 1,00,000 in ten years. The amount of the annual instalment or contribution can be ascertained by reference to Sinking Fund Tables.

When the money is required for repaying the liability or replacing the asset, the investments are sold and out of the sale proceeds the liability is repaid or the new asset is purchased. On the redemption of the liability the sinking fund is set free and may be used for providing depreciation of block or for any other purpose for which the profits of the company are available; but it must be remembered that it cannot be used for paying a dividend to shareholders because there will not be the necessary cash available for that purpose. It must, however, be pointed out that, if a sinking fund (called Capital Redemption Reserve Fund under the provisions of section 105-B) exists for the redemption of redeemable preference shares, it cannot be so used. It must remain as it is in the balance sheet, or else it can be employed only for issuing bonus shares to the shareholders. If a sinking fund is held for the purchase of a new asset, it will be used to wipe off the old asset, when a new asset has been acquired out of the sale proceeds of the investments.

The type of sinking fund described above is, theoretically speaking, the most perfect; but it must be clearly understood that, when such a sinking fund is set up, the following assumptions are made a number of years in advance :—

*(a)* That the profits of the company each year will be sufficient to permit the annual sinking fund contribution to be made;

*(b)* That there will be sufficient cash available each year to enable the sinking fund contribution to be invested outside the business, and

*(c)* That it will be possible year after year to make investments yielding the same rate of interest.

It is obvious that one or more of these assumptions may not hold good in future. For this reason, such a sinking fund is not one which can be conveniently adopted in practice; and in fact it is not employed by any company in this country. The sinking funds that are actually found in practice are therefore workable adaptations of what has been described above.

When a company issues long-term redeemable debentures, it may be required by the terms of their issue to contribute each year out of profits a certain sum towards a sinking fund for their redemption. If in any year the profits are not sufficient to enable the full sinking fund contribution to be made, the arrears may be carried forward to be provided out of future profits.

With regard to the investment of sinking fund contributions the company may have the option of either making outside investments or of utilising the sinking fund monies in its own business. Sometimes the sinking fund contributions, instead of being invested in securities, are used for repaying some of the debentures by drawing Where outside investments are made, the interest derived therefrom is credited to the sinking fund; but if the sinking fund is retained in

the business itself, the sinking fnnd may be credited each year with interest at a certain rate. In some cases bowever, the interest received from the sinking fund investments is not credited to the sinking fund but is credited to the company's profit and loss account.

If a company already holding a large portfolio of investments starts a sinking fund, there is no necessity of making fresh investments on account of the sinking fund, since tbe existing investments can very well be earmarked for that purpose. Where the sinking fund investments are specially earmarked, this fact is disclosed on the balance sheet.

**Requirements of Form F with regard to Reserve.** Tbe following information about the reserves of a company is to be disclosed in its published balance sheet —

Reserves

Any Sinking Fund

Any otber fnnd created out of net profits,
including any Development Fund

Any Pension or Insnrance Fnnd

Provision for Bad and Doubtinl Debts

These reqnirements of law may now be summarised as follows :—

1. The list of reserves given in Form F does not Include all kinds of reserves, nor is any distinction made between general and special reserves.

2. The balances of the various reserves are all that Is required to be shown In tbe balance sheet. It is not necessary to state the opening balances of the reserves and additions to and withdrawals from them separately, although this information is voluntarily given In many cases. Reserve operations (*i. e.*, additions to and drafts upon reserves), instead of being disclosed in the balance sheet, are sometimes indicated in the directors' reports, e. g.

'The General Development Reserve has been increased by Rs. 3,32,000 transferred from Debenture Redemption Fund, Rs. 7,000 profit on sale of investments and Rs. 1,00,000 set aside out of profits of the half-year, and reduced by a sum of Rs. 1,10,920 transferred in reduction of Block Account." *The Equitable Coal Co., Ltd.*— Directors' Report for the half year ended 30th June 1936.

3. Reserves are usually created out of profits by heing charged to the profit and loss account, but tbey may also be created out of other surpluses, as, for example, profit on the sale of investments may be transferred to Investment Reserve, unclaimed dividends transferred to General Reserve, unclaimed wages transferred to Workers' Relief Fund, or Stock Adjustment Reserve debited to sales.

4. In some companies specific reserves (such as 'Provision for Taxation' 'Provision for Pension' and the like) are not shown as such in the balance sheet, but they are included in 'Liabilities for other Finance' or 'Liabilities for Expenses.'

5. Capital reserves should appear separately from revenue reserves.

6. All reserve appropriations made by directors, under the power vested in them by the Articles, appear in the balance sheet prepared at the end of the year out of whose profits they are made; but the reserve appropriations made by shareholders on the recommendation of directors are shown in the balance sheet drawn up at the end of the next year, *i. e.*, the year in which such appropriations are actually made.

The information relating to reserves will now be illustrated by extracts taken from the actual published balance sheets of Indian companies.

**1. The Podar Mills, Ltd., Balance Sheet as on 30th September 1943.**

| | Rs. | a. | p. | Rs. | a. | p. |
|---|---|---|---|---|---|---|
| **Reserve Fund :—** | | | | | | |
| Balance as per Last Balance Sheet | 3,00,000 | – | – | | | |
| Amount added during the year | 4,00,000 | – | – | | | |
| | 7,00,000 | – | – | | | |
| *Less* Amount utilised for capitalisation and issue of 3,000 4% (free of Income-Tax) Cumulative Preference Shares of Rs. 100 each as fully paid. | 3,00,000 | – | – | 4,00,000 | – | – |
| **Reserve for Bad and Doubtful Debts:—** | | | | | – | – |
| Balance as per last Balance Sheet | | | | 11,000 | | |
| **Investment Reserve Fund :—** | | | | | | |
| Being the amount of excess realisation in respect of Investment sold during the year | | | | 2,37,496 | 12 | – |
| **Depreciation Fund :—** | | | | | | |
| Balance as per last Balance Sheet | 6,50,000 | – | – | | | |
| Amount added during the year | 3,50,000 | – | – | 10,00,000 | – | – |
| **General Welfare Fund :—** | | | | | | |
| Balance as per last Balance Sheet | 13,173 | 6 | 8 | | | |
| *Add* Amount set aside during the year .. | 5,000 | – | – | | | |
| Transfer of unclaimed wages up to 30. 9. 40 .. | 836 | 5 | – | | | |
| Cotton Charity Allowance and other credits ... | 2,458 | 7 | 6 | 21,468 | 3 | 2 |
| **Kodama Memorial Fund :—** | | | | | | |
| Balance as per last Balance Sheet | 1,050 | – | – | | | |
| Interest for the year ... | 52 | 8 | – | 1,102 | 8 | – |
| **Sasakura's Welfare Fund :—** | | | | | | |
| Balance as per last Balance Sheet | 2,100 | – | – | | | |
| Interest for the year ... | 105 | – | – | 2,205 | – | – |
| **Provision for Taxation —** | | | | | | |
| Balance as per last Balance Sheet | 4,92,980 | 15 | – | | | |
| Amount added during the year | 16,00,000 | – | – | | | |
| | 20,92,980 | 15 | – | | | |
| *Less* Taxes paid | 17,32,537 | 14 | – | 3,60,443 | 1 | – |

2. The Pankaja Mills, Ltd., B/S as on 31st December 1943

| | Rs. | Rs. |
|---|---|---|
| **Reserve Account :—** | | |
| Balance as per last Balance Sheet | 80,000 | |
| *Add* Amount transferred from mortgage Redemption Fund .. | 1,50,000 | |
| Amount transferred from previous year's profits ... | 1,20,000 | |
| Amount transferred from this year's profits ... | 4,00,000 | |
| | | 7,50,000 |
| Provision for Taxes ... | | 25,20,000 |

*Note.*—It appears from the above information that up to 31 st December 1924, transfers to the Reserve Accounts were made by shareholders on the recommendation of directors, but from 1943 the directors have been empowered to make such transfers.

3. The British India Corporation, Ltd., B/S, as on 31st December 1943

| | Rs | Rs. |
|---|---|---|
| **Reserves :—** | | |
| Capital Reserve ... | 20,00,000 | |
| General Reserve ... | 10,00,000 | |
| Rehabilitation Reserve ... | 15,00,000 | |
| Obsolescence Reserve ... | 15,00,000 | |
| Reserve against Loans ... | 1,54,201 | |
| Reserve for Renewals .. | 48,358 | |
| Reserve against Compulsory E. P. T Deposit .. | 30,00,000 | |
| Insurance Fund ... | 2,59,513 | |
| | | 94,62,072 |
| Taxation Reserve .. | | 1,59,36,039 |
| Provident Fund . | | 39,79,133 |
| *Reduction of Capital Account ... | | 43,172 |

* The Company's Share Capital was reduced by refunding a part of the paid up capital, and the 'Reduction of Capital Account' represents the amount not yet claimed by shareholders.

4. The Ryam Sugar Co., Ltd.—B/S. as on 30th June 1940

| | | Rs. | Rs. |
|---|---|---|---|
| **Reserves—** | | | |
| General .. | 4,01,640 | | |
| *Add* amount transferred from Unclaimed Dividends | 1,200 | | |
| | | 4,02,840 | |
| Taxation ... | | 12,412 | |
| Renewals and Improvements ... | | 99,634 | |
| Book Debts and Advances ... | | 43,690 | |
| Investments ... ... | | 2,500 | |
| Stores ... ... | | 36,302 | |
| | | | 5,97,378 |

5. The Burrakur Coal Co., Ltd.—B/S. as on 31st December 1940

| | | Rs | Rs. |
|---|---|---|---|
| Capital Fund ... ... | | | 30,00,000 |
| Reserves— | | | |
| General Reserve | | | |
| As per last Account | 49,71,709 | | |
| *Add* Amount transferred from Investment Reserve | 1,75,938 | | |
| | 51,47,647 | | |
| *Less* Amount trasferred to Capital Fund | 30,00,000 | | |
| | | 21,47,647 | |
| Equalisation of Dividend Reserve ... | | 30,000 | |
| Stock Adjustment Account ... | | 35,000 | |
| | | | 22,12,647 |

6. The Dunlop Rubber Co., (India) Ltd —B/S. as on 31st December 1940

| 1939 Rs. | | Rs. | Rs. |
|---|---|---|---|
| | Reserves— | | |
| 4,30,000 | General Reserve | 4,30,000 | |
| 5,00,000 | Reserve for Contingencies | 5,00,000 | 9,30,000 |
| | Provisions— | | |
| 13,16,449 | Taxation Reserve | 35,64,531 | |
| 50,000 | Gratuity Scheme Reserve | 50,000 | |
| | | | 36,14,131 |

7. The Bombay Dyeing & Mfg. Co, Ltd—B/S. as on 31st December 1940

| | Rs. | Rs. |
|---|---|---|
| Reserve ... ... | | 93,84,718 |
| Funds created of net profits : | | |
| Machinary Deterioration Fund ... | 2,00,38,282 | |
| Repairs Fund (Building Depreciation) ... | 63,14,179 | |
| Dividend Equalisation Fund ... | 8,74,000 | |
| Fire Insurance Fund ... ... | 11 66,275 | |
| | | 2,83,92,736 |
| *Other Funds : | | |
| Workmen's Welfare Fund ... ... | 83,119 | |
| Fines Fund ... ... | 7,245 | |
| | | 90,364 |
| Provision for I. T. and S. T. ... ... | | 3,34,540 |

* Probably created as follows :—

"Workmen's Welfare Fund" by transfer of unclaimed wages and "Fines Fund" by transfer of fines imposed on workmen.

8. The Associated Cement Co., Ltd., B/S. as on 31st July 1940

| Previous year Rs. | | Rs. | Rs. |
|---|---|---|---|
| | **Debenture Redemption Fund :—** | | |
| 2,20,769 | As per last Account ... | 3,21,169 | |
| 100,,400 | Addition during the year | 1,06,919 | |
| | | | 4,28,088 |
| 3,21,169 | | | |
| | **Reserve Fund :—** | | |
| 39,00,000 | As per last Acconut ... | | 39,00,000 |
| | **Insurance Fund :—** | | |
| 14,598 | As per last Account ... | 30,526 | |
| 26,467 | *Add* Amount appropriated from dnring the year | 21,988 | |
| 41,065 | | 52,514 | |
| 10,539 | *Less* Payments ... | 5,652 | |
| | | | 46,862 |
| 30,526 | | | |
| | **Workmen's Welfare and Benefit Fund :—** | | |
| 24,549 | As per last Account ... | 26,051 | |
| 1,502 | Nett additions during the year including Interest earned on Government Securities as per contra ... | 1,256 | |
| | | | 27,307 |
| 26,051 | | | |
| | **Reserve for Income Tax and Super Tax** | | |
| 40,65,000 | As per last Acconnt | 33,01,918 | |
| 10,37,000 | *Add* Provision made this year ... | 8,04,000 | |
| 51,02,000 | | 41,05,918 | |
| 18,00,082 | *Less* Payments for the year 1939 40 ... | 22,06,881 | |
| | | | 18,99,037 |
| 33,01,918 | | | |

9. The Titaghur Paper Mills Co., Ltd.—B/S. as on 31st March 1941

| | Rs. | Rs, |
|---|---|---|
| Reserve ... ... | | 8,06,359 |
| Debenture Redemption Reserve ... | | 2,50,000 |
| Reserve for Revaluation of Stocks and Stores | | 5,50,000 |
| Provision for Taxation ... ... | | 38,26,303 |
| Reserve for Discoonts ... ... | | 2,91,721 |
| Reserve for Labour Quarters and Labour Welfare ... ... | 2,54,952 | |
| *Less* Expenses ... ... | 7,586 | |
| | 2,47,366 | |
| Since added ... ... | 50,000 | |
| | | 2,97,366 |

| | | | |
|---|---|---|---|
| Provision for Bad and Doubtful Debts | ... | | 3,52,923 |
| *Provision for Indian Worker's Pension | ... | | 30,000 |
| *Provision for Indian Staff Pension | ... | | 10,000 |

* These do not appear as such in the B/S, but they are included in the item "Liabilities for other Finance" they are new reserves created for the first time this near, and their existence is ascertained from the P. & L. a/c

**10. The Tata Hydro-Electric Power Supply Co. Ltd., B/S as on 30th June 1940**

| As at 30-6-39 | | Rs. | Rs. |
|---|---|---|---|
| | Reserves :— | | |
| 2,85,468 | General Reserve Fund | 6,35,469 | |
| | Depreciation Fund:— | | |
| | Balance as at 30 6 39 1,06,68,638 | | |
| | *Less*: Cost (less salvage value) of assets sold or scrapped 1,18,188 | | |
| | 1,05,50,450 | | |
| | *Add* Provision made this year 3,00,000 | | |
| 1,06,68,638 | | 1,08,50,450 | |
| 2 09,578 | Reserve for Special Repairs | 2,41,081 | |
| 75,000 | Reserve for Doubtful Debts | 75,000 | |
| 11,12,900 | Reserve for I. T. and S. T. | 12,06,776 | |
| | | | 1,30,11,776 |
| 1,23,51,584 | | | |

**11. The Indian Iron and Steel Co, Ltd.—B/S. as on 31st March 1940**

*Schedule B—Reserves*

| | | Rs. | Rs. |
|---|---|---|---|
| Capital Reserve · | | | |
| Balance as at 31-3-1939 | . | | 17,33,421 |
| Surplus on Conversion : | | | |
| Profit on Conversion of 4% Convertible Second mortgage Debentures :— | | | |
| Balance as at 31-3-1939 | ... | 20,38,500 | |
| Added during the year | ... | 18,760 | |
| Premium on Shares : | | | 20 57,260 |
| *Balance as at 31-3-1939* | ... | | *62 92,020* |
| Repairs and Renewals Reserve : | | | |
| Provision as at 31-3-1939 | ... | 23,40,495 | |
| Set aside during the year | ... | 8,86,960 | |
| | | 32 27,455 | |
| *Less* Expenditure during the year | ... | 7,02,736 | 25,24,719 |
| Workmen's Compensation | ... | | 60,444 |
| Provision for I. T. and S T. | ... | | 53,41,202 |
| Total Rs. | | | 1,80,09,066 |

*Notes*—1. There is also a "Dividend Adjustment Account" for Rs. 25,50,000, which appears separately from Reserves

2. In publishing its Balance Sheet, the company has made use of schedules as permitted by form F.

12 The Shivrajpur Syndicate, Ltd., B/S. as on 30th November 1940

| | Rs. | Rs. |
|---|---|---|
| Reserve Funds :— | | |
| General as per last B/S ... | | 3,25,000 |
| Mine Development and Prospecting | | |
| As per last B/S .. | 1,65,413 | |
| *Less* Transferred from Development Work in-Progress a/c ... | 7,413 | 1,58,000 |
| Equalisation of Dividends as per last B/S. | 1,40,000 | |
| *Less* Transferred to P & L a/c ... | 35,000 | 1,05,000 |
| Workmen's Compensation as per last B/S. | 30,255 | |
| *Less* Paid during the year | 2,293 | 27,962 |
| Bonus | | |
| As per last B/S ... | 7,744 | |
| *Less* Paid during the year ... | 795 | 6,949 |
| *Doubtful Debts ... ... | | 83,854 |

*Created this year as shown by the P. & L. %

### 3. DEBENTURES AND LOANS

**Borrowing Powers of a Company.** A trading company has an implied power to borrow, if such borrowing is properly incidental to the conduct of its business. Such power is, however, expressly taken in the memorandum of association. In the case of non trading companies the law does not give an implied power to borrow. A non-trading company must therefore have express power in its memorandum before it can borrow. When a company can borrow it can also pledge its property as security. A limit is usually placed on the amount to be borrowed either by the memorandum or by the articles

A company may pledge the whole of its property and undertaking, both present and future, as security for loans, where it has an express or implied power to borrow. If it desires to pledge its uncalled capital, it should have express power in its memorandum or articles to do so. The uncalled capital cannot, however, be pledged under any circumstances where it has been specially earmarked as reserved capital under section 69 of the Indian Companies Act; nor can a banking company, under section 277J, create any charge upon its unpaid capital.

The articles will provide whether the power to borrow is to be exercised by the company in general meeting or whether the power shall be vested in the directors. The usual plan, however, is for the directors to be authorised to exercise the borrowing powers of the company up to a certain limit, and that limit is not to be exceeded except with the sanction of the company. The limit may be the amount of the nominal capital of the company for the time being or any other sum. Under section 87G of the Indian Companies

Act, a managing agent cannnt exercise in respect of any company of which he is a maoaging agent a power to issue debentures.

Section 103 of the Indian Companies Act provides that a company caonot exercise its borrowing powers nntil it has received a certificate entitling it to commence bnsiness, but that a company may nevertheless, *before it obtains such a certificate*, offer shares and debentnres simnltaneously for public sobscription, may allot shares and debentures and receive mnney payable on application for debentures. This restrictinn does nnt apply to private companies which may exercise their borrowing power as soon as they are incorporated.

A company may borrow in the shape of short-term or long-term loans according to its needs. Short-term loans are nsually taken from banks; but long term borrowing may be either by means of mortgages on its property or, as is more usnal, by an issue of debentures.

**Debenturea.** A debenture is a mere acknowledgment of indebtendness given uoder tbe seal of the company containing a contract for the repayment of the principal sum at a specified date and for the paymeot of interest (nsually half-yearly) at a fixed rate per cent. until the principal snm is repaid, and may or may not give a charge on the assets nf tbe company as secnrity for the loan.

Many forms of debentnres exist, and the term is somewbat loosely applied in bnsiness, but the following observations should be read in conjunction witb the foregoing definition ;—

1. A debeoture, as a rule, is one of a series which are expressed to rank *pari passu* with each other as to any charge given by tbe debeoture; but a single debentnre may be issned. If the debentures of a series are not made to rank *pari passu* they wnuld rank according to the date of issue or if issned on tbe same day in nnmerical order. The company cannot create new series of debeotnres to rank *pari passu* with the old unless the right has been specifically reserved.

2. Debentnres are not confined tn companies alone; but clnbs, municipal corporations, port trnsts and nther public bodies very often issue them.

3 Debentnres usnally provide for the repayment of tbe priocipal sum on a fixed date, usnally five, ten or twenty years after issue, or they may be repayable no demand, or they may be irredeemable They can be made perpetual in the sense that there need be no fixed time for paying them off. Section 126 of the Indian Companies Act permits the issne nf irredeemable debeotures, although in practice such debentures are nnknown.

4. The rate of interest payable is usually specified to be at a fixed rate per cent., but it need nnt be so The capital sum may carry oo interest and the debentnre may be issued at a discount and the capital snm be expressed to be repaid at par or at a permium. The interest payable may also be made to vary witb the profits, or provision may be made in the debentnre to the effect that the

interest shall only be payable out of profits and such interest may be cumulative or non-cumulative.

5. Debentures may or may not give a charge on the property, assets or undertaking of the company. Where they do so give a charge they should always be referred to as Fixed Mortgage Debentures if the charge is fixed or Floating Mortgage Debentures if it is not fixed.

6. Debentures giving a charge on the property of the company may or may not also be secured by the creation of a trust deed vesting the property in trustees upon trust, such trustees having power on the default of the company to seal the assets and pay off the debentures.

**Debenture Stock.** Debenture stock is a term used to denote the capital sum lent to a company, which is usually secured by a trust deed creating a mortgage or charge in favour of the trustees upon the property forming the security. The capital sum or stock is by the terms of the trust deed divided into units, in respect of his holding of which each stockholder is entitled to a certificate. The trust deed provides for a register of holders being kept, and for transfers of the stock in certain fractions, and usually contains provisions for repayment of the stock and for enforcing the charge. The incidents of debenture stock are for practical purposes the same as those of debentures and the holders of the stock occupy a position very similar to that of the holders of debentures.

**Status of Debenture-holders.** A debenture holder is a creditor of the company, and is entitled to interest at a specified rate whether profits are earned or not except when he holds what is known as an income debenture in which case interest is payable only out of profits. He therefore differs from a shareholder in that the latter is a member of the company whose income comes solely out of profits A debenture-holder usually possesses a security for his loan whereas a shareholder has no security. A debenture-holder is not, however, entitled to anything more than his fixed interest, however big the profits of the company may be.

**Security for Debentures** A company may issue debentures without any security (known as naked debentures); but usually a company's assets are charged as security in favour of the debentureholders. The security may be in the form of a specific mortgage or a floating charge or a combination of both.

When debentures are secured by a charge on the company's property, the charge may be created by words in the debenture itself, or by a deed the benefit of which the debenture holders are declared to be entitled to, or by a combination of both these methods.

**Trust Deed.** When debentures are issued for public subscription, a trust deed is invariably executed in favour of the debenture holders, a trustee or trustees being appointed and remunerated by the company to act on behalf of the debenture holders. The trust deed contains, *inter alia*, the following clauses :—

1. Particulars of the property charged as security, and whether by specific mortgage or floating charge or both.

2. Whether the company shall have power to create any mortgage having priority to the charge inclnded in the deed.
3. Provision for redemption of the debentures, including the price and date or dates at which they shall be redeemed, and whether by drawings, purchase in the market, or by ordinary redemption. If a sinking fund is to be created out of profits to provide for redemption, details of this will be included in this clause.
4. Powers of trustees to deal with the assets charged as security in the event of default by the company in payment of interest, or repayment of capital or upon a winding up.
5. Whether the debentures shall be registered or bearer form and the manner of their transfer.

When a trust deed is in existence, the debentures themselves should contain a clause incorporating its terms by reference. By section 125 (2) every debenture holder has the right to a copy of any trust deed for securing the debentures he holds on payment of a sum not exceeding one rupee in the case of a printed trust deed or on payment of six annas for every hundred words required to be copied where the trust deed has not been printed.

The trustees appointed by the company to look after the interests of the debenture holders may be individuals or a corporate body. Banks, share brokers, lawyers, insurance companies and investment trusts usually act as trustees.

The most important advantages to be obtained from securing the debentures by the creation of a trust deed are :—

1. The property charged actually vests in the trustees ; and
2. The trustees can enter and sell immediately on default, and can continually watch over the interests of the debenture holders and, if necessary, force the company to keep the property charged in good condition. In the absence of trustees, valuable time is usually lost by waiting for some debenture holder to take action.

It is clear that for the absolute protection of the security in the case of a fixed charge the title deeds of freehold property or leases if the property is leasehold, should not remain in possession of the directors, since further charges ranking in priority to the debentures might be created. It is not possible, however, to give the security to each debenture holder and trustees are therefore appointed to represent them

The trustees must carry out their duties under the trust deed honestly and must not commit any breach of trust therein contained, for they have the liability of and are in the same position as other trustees. They are appointed and their remuneration is fixed by the deed. If no provision is made in the deed for remuneration they are not entitled to any.

Under section 146 of the Indian Companies Act, the trustees for debenture holders have the same right to receive and inspect the balance sheets and profit and loss accounts of the company and the

reports of the anditors and other reports as is possessed by tbe holder of ordinary sbares in the company.

**Fixed Mortgage.** A fixed cbarge consists of an actual mortgage of the assets of the company nsually to trnstees for debenture holders, thereby preventing the company from creating charges in priority to the fixed charge.

The fixed charge is nsually restricted to wh it are known as fixed assets. The company cannot deal with the assets that have a fixed charge upon them. No fixed charge is, therefore, created on floating assets of tbe company.

**Floating Charge.** Debentnres may be issned giving a floating cbarge on the assets and/or undertaking, both present and future, of the company as security for the debentures.

A floating cbarge does not prevent the company from dealing with the property so charged in the ordinary conrse of business. It may embrace moveable property as well as fixed property, and the property so included may change its character in the conduct of the company's business For example, stocks will automatically change to debtors' balances and cash ; debtors' balances will liquidate into cash, and casb will be expended in new stocks, etc. Uncalled capital and futore property are frequently contained in the charge. Not until a floating charge becomes fixed, or as it is often terms, 'crystallises' is the company precinded from disposing of the assets involved. The circumstances in which a floating charge crystalises (e. g., failnre on tbe part of the company to pay interest on the due dates or neglect to satisfy the provisions as to redemption) are ennmerated in the debentures or the trust deed.

**Fixed v. Floating Charges.** The advantage of a fixed charge over a floating cbarge lies in the fact that the debentnre holders know to which particular assets they may look for security, if the need arises Against this, the security afforded is restricted to specific assets which may shrink in value. Buildings erected for the special purposes of tbe business are often saleable only at considerable loss.

When debentures are secured by a floating charge, the holders may rely upon any assets inclnded in the charge for satisfaction of tbeir claims, even though certain assets may not bave been in existence at tbe time the charge was created. On the other hand, a risk is always present that in the event of a prolonged period of depression ensuing, a company's assets may become partially consumed in an attempt to avert financial disaster. This eventuality would result in a contraction of the security furnished by a floating charge. The widest security is not therefore necessarily tbe best, and each should be valued on its merits

"A floating security is an eqnitable charge on tbe assets for the time being of a going concern ; it attaches to the subject charged in tbe varying condition in which it bappens to be from time to time. It is the essence of such a charge that it remains dormant until the undertaking charged ceases to be a going concern, or until the person in whose favour the charge is created intervenes. His right to intervene may, of course, be suspended by agreement. But if there

is no agreement for suspension he may exercise his right whenever he pleases after default."

It is Important for investors to remember that floating debentures do oot give a paramonnt security for the fnllowing reasons :—

1. The company is free to create specific mortgages on the property charged in the floating debenture having priority over such debenture unless otherwise agreed in the terms of the issue of the floating debenture that the company shall not be at liberty to create any charge baviog priority over them.

2 By sectinn 233 of the Indian Companies Act a *floating* charge created within tbree months nf the commencement of winding up will only be effective to the extent nl tbe amount then actually advanced to the company with interest at five per cent. unless the company was solvent at the time the charge was given.

3. Under section 129 of the Act, if a receiver is appoioted In respect of debentures secured by a floating charge or possession is taken by or on behalf of snch debentnre holders and the company is not In the conrse of winding up, then the receiver or other person taking possessiuo must pay out of the assets coming into his hands the debts which are by section 230 prelerential in priority to the principal or Interest In respect of the debentures.

The difference between a fixed and a floating charge ls clearly brought ont in the following extract from a jndgment :—

"A specific charge, I think, is one tbat withont more, fastens on ascertained and definite property or property capable of being ascertained and defined ; a floating charge, on the other hand, is ambulatory and shifting in its nature, hovering over and so to speak floating with the property which it is intended to affect until some event occnrs or some act ls done which causes it to settle and lasten on the subject of the charge within its reach and grasp."

The following extracts from company prospectnses illustrate typical debenture securities :—

"Six per cent. Debentnres of the total amonnt nf Rs 3,00 000 divided into 300 bearer debentures nf Rs 1,000 each will be issued *and the amount will be secured by a mortgage and* charge on *all* the properties and assets of the company including its uncalled share capital. "*The Atal Tea Company (1943), Ltd.*, Prospectns dated 22nd January 1943.

"The debentures will be secured by a first mortgage to trnstees for debentnre holders on the immnveable properties of the company and by a floating charge on all the nther general assets ol the company, *The Velimalai Rubber Cn., Ltd.*—Prospectns dated 7th March 1944.

**Issue nf Debentures.** Debentures, unless privately taken up by the managing agents, directnrs and their friends, are usually offered to the public by means of a prnspectns, which must include all the information relevant to the company and to the debentures as required by section 93 of the Indian Cnmpanies Act.

Debentures may be issued to a creditor in respect of an existing debt or a fresh loan or as collateral security. They are, however, usually offered for public subscription in the same way as shares and afford a prospective investor an alternative form of investment in the company.

They may be issued like shares at par, at a premium or at a discount. Sometimes debentures may be issued at a considerable discount but no interest may be payable thereon for some time. Thus Belsund Sugar Co., Ltd., issued in 1934 Rs. 10,00 000 Debentures of Rs. 100 each at Rs 80 per debenture, carrying no interest for the first two years but thereafter at the rate of 5½ per cent. per annum. The interest attached to debentures must be paid after deduction of income-tax; but a company may issue debentures carrying interest free of tax, in which case the income-tax on debenture interest will be payable by the company. The Portland Rubber Estates, Ltd, issued in 1944 4,000 first mortgage debentures with rights of bearer bonds of Rs. 100 each, carrying 5% per annum interest tax free. The Consolidated Coffee Estates (1943), Ltd, Velimalai Rubber Co, Ltd., Amalgamated Coffee Estates, Ltd., and a few other South Indian plantation companies have also issued debentures carrying tax-free interest.

Where debentures have been issued at a discount and where any commission is paid on their issue, the following publicity has to be given to these facts:

Section 106 makes it obligatory for a company to show any sums paid by way of commission and any sums allowed by way of discount on debentures in every balance sheet until the whole amount has been written off.

Under section 111, particulars of any commission or discount paid on debentures must also be filed with the Registrar along with the particulars of mortgages and charges.

Any expenses incurred in connection with the issue of debentures so far as they are not written off, must be shown under a separate heading in the balance sheet.

*N. B.*—A contract with a company to take up and pay for any debentures of the company may be enforced by a decree for specific performance as laid down in section 126.

**Registered and Bearer Debentures.** A registered debenture is one whose holder is registered in the books of the company. The object of issuing registered debentures is to meet the requirements of the money market and to facilitate dealings. It simplifies the title and enables the company to look to some specific person as the holder to whom it can make payments, and whose receipt is to be a sufficient discharge.

Although a company is not bound to keep a Register of Debenture holders, yet in practice one is usually maintained in which to record the names, addresses, occupations and amounts of holding of each debenture holder. This register is dealt with and written up in the same manner as the Register of Members. If a register of debenture holders is kept section 125 requires that it must be open to the

inspection of members and debenture holders during at least two hours a day. There is a heavy penalty for refusing inspection.

Registered debentures are transferred in the manner specified in the conditions endorsed thereon—usually by means of a transfer deed. A company can become a transferee of its own debentures, and the same debentures may be reissued as explained later on.

Alternatively, a debenture may be in 'bearer' form, i. e., transferable by mere delivery. The interest due is paid to the holder irrespective of his identity, at each interest date. Coupons are frequently attached to bearer debentures for presentation through a bank on the due dates.

A bearer debenture is therefore possessed with the attributes of a negotiable instrument i. e., its legal ownership passes by mere delivery, no written transfer being necessary to invest it in a purchaser.

Some companies issue bearer debentures in the first instance but they give to the holders the option of converting their debentures into registered one if they so desire

**Redemption of Debentures.** Under section 126 a company can issue irredeemable or perpetual debentures but such debentures are almost unknown in practice. Debentures are invariably redeemable, and the date on or before which they must be redeemed is stated in the terms of issue. The provision for the redemption of debentures is usually made by one or more of the following methods :—

1. On a specified future date, with an option entitling the company to redeem (either in part or in whole) on or after a stated earlier date.
2. By purchase in the market at or below a certain price either at any time, or on or after a specified date.
3. By drawings, either at fixed intervals, or at the company's option on or after a specified date.

In addition, the redemption may be at a price corresponding with the price of issue, or may be at a higher price, or may vary according to the particular option which the company may exercise.

The object of a company reserving to itself at least two alternatives, either as to date or as to price, or both, is to enable it to choose the most favourable time to redeem the loan, having regard to the state of its own credit and external monetary conditions.

When powers are taken by a company to purchase in the market at or under a specified price, an alternative must always be provided (e. g., drawings at that price), since the market quotation may be in excess of the stipulated maximum.

Companies sometimes provide for the creation of a sinking fund out of which the debentures are to be redeemed. Unless stated to be "out of the profits of the company" such sinking fund is a charge against receipts and must be provided for whether profits are earned or not.

**Convertible Debentures.** In some cases an option is given to debenture holders to exchange their debentures for shares. Such a

provision gives an investor the privilege of coming in with the status of secured creditor and retaining that relationship to the company until such time as profits appear to be sufficiently high to justify changing his status to that of a shareholder. He is thus able to retain the advantage of having his money secured on the assets until the company is in a sound financial position although it must be realised that once he has elected to exchange his debentures for shares, he has no right subsequently to revert to the capacity of debenture holder.

**Registration of Mortgages.** By section 109, every mortgage or charge created by a company and being either—

*(a)* a mortgage or charge for the purpose of securing any issue of debentures ; or

*(b)* a mortgage or charge on uncalled share capital of the company or

*(c)* a mortgage or charge on any immoveable property wherever situate, or any interest therein ; or

*(d)* a mortgage or charge on any book debts of the company ; or

*(e)* a mortgage or a charge, not being a pledge on any moveable property of the company except stock in-trade ; or

*(f)* a floating charge on the undertaking or property of the company ; shall, so far as it contains a charge, be void against the liquidator and creditors of the company, unless it is delivered for registration with the Registrar within twentyone days of its creation.

In addition to the registration of mortgages and charges with the Registrar, the company must keep (*i*) a register of mortgages and charges specifically affecting the property of the company (section 123); and (*ii*) copies of all mortgages and charges which have to be registered with the Registrar (section 117). Section 124 further provides that both these shall be open to the inspection of any creditor or member without charge, and the register available for the inspection of any other person on payment of a fee not exceeding one rupee.

The various terms on which debentures are issued by companies and also the several privileges that may be attached to debentures have been discussed above. Below are given a few examples of the actual terms and conditions on which debentures have been issued by certain companies in India.

1. **The Velimalai Rubber Co, Ltd**—Prospectus dated 7th March 1944.

The debentures constitute but $33\frac{1}{3}$ per cent of the total funds to be raised and will be redeemed over a period of six years from the 1st January 1950 on the terms and conditions as provided hereunder :—

*(a)* The debentures will be issued in the form of bearer bonds and will carry interest at the rate of 6 per cent (free of tax) calculated from the date of allotment.

*(b)* Such interest will be paid half-yearly, on the 30th of June and 31st of December every year, the first of such payments to be made on the 31st December 1944.

*(c)* The debentures will be secured by a first mortgage to Trustees for Debenture Holders, on the immovable properties of the Company, and by a floating charge on all the other general assets of the Company

*(d)* No further issue of the debentures will be made ranking in priority to or pari passu with the present issue of Rs 3,75,000.

*(e)* One of the Debenture Trustees shall ex-officio be a director of the company.

*(f)* The redemption terms are as follows :—*(i)* The debentures are not redeemable until Ist January 1950 ; *(ii)* towards the amortisation of debentures a Sinking Fund will be created to which a sum of not less than Rs. 20,000 will be contributed annually from the profits of the company from 1946 ; *(iii)* on and after the Ist January 1946, however, the Directors will have the option to purchase from the market for cancellation any or all of the debentures as they become available, either at a discount, at par, or at a premium utilising the amounts available out of the Sinking Fund for the purpose ; *(iv)* The remaining debentures either wholly or in part will be redeemed, at any time after Ist January 1950, at the discretion of the directors, at par, but not later than 31st January 1956 ; *(v)* Such redemption will be made in annual instalments. by drawing lots commencing from 1st January 1950, subject to the proviso that three months' prior notice is given of such drawings to the holders of debentures ending with an interest payment date.

*(g)* The trustees for the debenture holders are: J. R. Motishaw, Esq., of Messrs. J. R. Motishaw & Co., Stock, Share and Finance Brokers, Apollo St., Bombay ; and K. C. Thomas, Esq., B. A., Karottu House, Kottayam.

**2 The Belsund Sugar Co., Ltd**

In 1934 the Company issued Rs 10,00,000 Debentures of Rs. 100 each at Rs. 80 carrying on interest for the first two years but thereafter at the rate of 5½ per cent. per annum (taxable), repayable on 30th September 1944 at par or at the option of the Company at any time on 6 months' notice.

The holder of each debenture has the option to subscribe at any time for an allotment of ordinary shares of Rs. 7-8 0 each for an aggregate nominal value of Rs. 90 payable in cash, and this option expires at the end of 3 months from the date of the notice of repayment by the Company.

Interest payable 31st March and 30th September.

The debentures are registered and are transferable by deed only.

**3. The Bharat Sugar Mills. Ltd.**

The Company issued at par in July 1932 Rs. 2,50,000 debentures in 8% (taxable) bearer bonds of Rs. 500 each, repayable at par in July 1937.

Out of the above debentures Rs 1,25,000 were paid off after Ist July 1937, and the remaining debentures for Rs 1,25,000 were continued at the reduced rate of interest 4½ per cent., repayable in whole or in part at the option of the Company, at any time after Ist July 1938 on two months' notice. Interest payable on Ist July.

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4 The Samastipur Central Sugar Co., Ltd

The Company issued at par on 1st October 1935 Rs. 4,00,000 in 5 per cent. (taxable) bearer bonds of Rs. 500 each, repayable at par on 1st October 1955, with the option of repayment at a premium of 3 per cent. on 1st October 1945 or any subsequent 1st October before 1st October 1955 on three months' notice, if the whole amount is intended to be redeemed ; if not drawings will be made at least one month before the date of redemption and 10 days' notice of such drawings will be given

Interest payable on 1st April and 1st October.

The Company shall in each year set apart out of the profits Rs. 20,000 to form a sinking fund for the repayment of the debentures. If in any year the profits do not suffice to provide this sum, the deficiency shall be made good from the profits of the succeeding year or years.

5. The Tezpore Tea Co., Ltd

The Company issued at par on 1st October 1932 Rs. 5,00,000 in 7 per cent. (taxable) bearer bonds of Rs 500 each, repayable at par on 31st December 1971 with the option of repayment at par, in whole or in part, at any time after 31st December 1935 on six calendar months' notice if the bearer has not validly exercised his option to exchange the bond for ordinary shares.

The holders of these debentures have the right, after 31st December 1935 but before 31st December 1949 to convert them into ordinary shares; six months' notice of intention to convert must be given, each Rs. 500 Debenture being convertible into 50 ordinary shares of a denomination of Rs. 10 each fully paid up.

Interest payable on 30th June and 31st December.

6. The Tata Chemicals, Ltd.

The Company issued in January 1942 at par Rs. 35,00,000 in 4 per cent. (taxable) bonds of Rs. 100, Rs. 1,000 and Rs. 10,000 each, repayable at par on 15th January 1952 with the option of repayment in whole or in part at par on or after 15th January 1948, on six months' notice.

Interest payable on 15th July and 15th January.

These debentures are bearer bonds capable of registration on the request of the bearer on payment of a registration fee of Re. 1 for each registration, with the right to re-convert registered debentures to bearer bonds.

Debentures of Rs. 100 and/or Rs. 1,000 each may be consolidated into debentures of Rs. 1 000 and Rs. 10,000 each and debentures of Rs. 1,000 and Rs. 10,000 each may be subdivided into debentures of Rs. 100 and Rs. 1,000 each.

A debenture holder may exercise one of the following alternative options in respect of each unit of Rs. 100 each held by him.

*(a)* Between 1st January 1943 and 30th June 1943 to exchange the unit for 8 ordinary shares of Rs. 10 each fully paid up;

*(b)* Between 1st January 1944 and 30th June 1944, on payment of Rs. 8 in cash, to exchange the unit for 8 ordinary shares of Rs. 10 each fully paid up ; and

*(c)* Between 1st January 1945, and 30th June 1945, on payment of Rs. 10 in cash, to exchange the unit for 6 ordinary shares of Rs. 10 each *fully* paid up.

**7. The Indian Iron & Steel Co., Ltd.**

In December 1936 the Company issued at 98 per cent. £1,500,000 *First Mortgage Debentures in 4 per cent.* Bonds of £100 and £ 50 each, redeemable by the operation of a cumulative sinking fund of 1½ per cent. per annum, commencing in 1941, which will be applied in purchases at any price less than par (exclusive of accrued interest) or by annual drawings at par ; with the option of redemption in whole or part on any interest date after 31st December 1951, at a premium of 2 per cent. on six months' notice. Any of the debentures not previously redeemed will be repayable at par on 31st December 1966.

Interest payable 1st January and 1st July. These debentures are registered and are transferable by deed only.

The Company also issued in December 1936 at par £500,000 onvertible Second Mortgage Debenture Stock, repayable at par on 31st December 1961, but may be redeemed in whole or part, at a premium of 2 per cent. on six months' notice expiring on any interest date after 31st December 1943.

Holders of the Convertible Stock may at any time up to and including 1943 convert into fully paid ordinary shares at the rate of one ordinary share of Rs. 10 for every £1 10s. of Convertible Stock. All ordinary shares so issued will rank for dividend for the financial year following that current at the date of the exercise of the option and the holder will receive interest on the stock converted in respect of the financial year in which the option is exercised

**8. The Steel Corporation of Bengal, Ltd.,**—Ibid p. 383.

£ 1,000,000 (Rs 1 33,33,333) 4½ per cen. Guaranteed Convertible Registered *Mortgage Debentures* of £ 50 each (unconditionally guaranteed as to principal and interest by the Indian Iron & Steel Co., Ltd.), issued at par in *May* 1937, repayable at par on 1st *January* 1957, but may be redeemed in whole or in part, at a premium of 2 per cent. on six months' notice expiring on any interest date after 1st January 1947.

Holders of the fully paid up convertible debentures may at any time up to 1st January 1947 convert into fully paid up ordinary shares, each £50 debenture for 40 ordinary shares of Rs. 10 each.

*Note.* Information contained in all the above examples except the first has been taken from "The Investor's *India Year Book*" for 1942–43 compiled by Messrs Place, Siddons & Gough, Calcutta.

### Other Creditorship Securities.

Besides debentures, there are a few other types of creditorship securities which are sometimes issued by companies to their creditors These are :—

**1. Income Certificates.** When the capital of a company is reorganised, income certificates may be issued to the cumulative preference shareholders in satisfaction of their claims in respect of past dividend arrears. Thus the Namburnadi Tea Co., Ltd., reorganised its capital in June 1937, when all arrears of cumulative preferential dividend were cancelled, and the holders of such shares were given in lieu thereof one income certificate of Rs. 100 for every 20 preference shares held by them. The income certificates carry interest at 5 per annum payable from profits from 1st January 1936.

The 5 per cent interest attached to these income certificates is noncumulative, but the certificates carry preferential claim to repayment of principal. They are repayable by annual drawings.

It will be seen that such income certificates are an intermediate security between preference shares and debentures. They partake of the nature of both, but they are neither preference shares nor debentures. They are after all creditorship securities. *The Investor's India Year Book 1942-43 p. 300.*

**2. Convertible Notes.** These are in fact a kind of naked debentures. They are also issued when a company's capital is reconstructed. Should it be desired to issue them to the public for cash subscription, no one would probably come forward to buy them. The Ramnugger Cane and Sugar Co., Ltd., issued in May 1941 Rs. 6,00,000 in 2½ per cent. convertible notes of Rs 1,000 each at a discount of 4 per cent., repayable on 31st May 1950 at a premium of 35 per cent. Interest payable on 31st May and 30th November each year.

In a winding up or in failure to pay interest or otherwise to comply with the terms and conditions on which these notes were issued they shall be liable to be repaid at a premium of 4 per cent, if repaid on or before 31st May 1942. In the event of these becoming repayable after 31st May 1942 but before 31st May 1950 the same will be repaid at a premium of 4 per cent plus an additional Re. 1 per cent. for every completed period of 3 months as from 31st may 1942.

At any time on or after 1st June 1942 the holder of any note shall have the option to require the Company to issue to him or his nominee such number of ordinary shares of Rs. 10 each at par as would be equivalent in nominal amount to the sum at which his note would be repayable, if it had fallen due for repayment on the date of the exercise of his option, the ordinary shares thus issued ranking *pari passu* with the existing ordinary shares in respect of subsequent financial years. *The Investor's India year Book 1942-43 p 354.*

**3. Deposit Certificates** They are like promissory notes and may be issued by a company in satisfaction of a debt due from it. The Tata Iron & Steel Co., Ltd., issued in July 1942 3% bearer deposit certificates in part payment of the dividend due to its ordinary and deferred shareholders. These certificates were repayable in three years, but they were actually paid off earlier.

**Requirements of Form F with regard to Debentures and Loans.** The balance sheet of a company must disclose the following information relating to debentures and loans :—

Debentures stating the nature of security

Loans :—

*(a)* Secured—

(*i*) Loans on mortgages or fixed assets

(*ii*) Loans on debentures

(*iii*) Loans from banks stating the nature of security

(*iv*) Liabilites to subsidiary companies

(*v*) Other secured loans stating the nature of security

(*vi* Interest accrued on mortgages, debentures or other secured loans

*(b)* Unsecured—

(*i*) Loans from banks

(*ii*) Fixed deposits

(*iii*) Short-term loans

(*iv*) Advances by directors or managers and managing agents

(*v*) Interest accruing but not due and interest accrued and due

(vi) Liabilities to subsidiary companies

The above-mentioned requirements of law may be explained as follows :—

1. First of all it should be noted that debentures are illogically mixed up with reserves in Form F. They should have been given above loans.

2. All that is required is the amount of outstanding debentures together with the nature of security given in respect of them. It is not necessary to show separately the amount of debentures issued and those redeemed during the year, although some companies follow this practice.

3. Debentures issued as collateral security for a secured loan may be shown either along with debentures or under the heading 'Secured Loans'.

4. Any interest accrued on debentures is to be given either with debentures or under the heading 'Secured Loans'.

5. If on the date of the balance sheet there are any debentures that have been redeemed but for which payment has not been claimed, they should not be shown either as debentures or as loans. They must be given either as a separate item (Unclaimed Debentures) or under current liabilities.

6. Liabilities to subsidiary companies (both secured and unsecured) are to be detailed separately.

The following examples will illustrate how debentures and loans are disclosed in the balance sheets of Indian companies :—

**1. The Ryam Sugar Co., Ltd., B/S. as on 30th June 1940**

| | Rs. | Rs. |
|---|---|---|
| 7% Mortgage Debenture Bonds (Secured on Land, Building, Machinery, Stores and Book Debts) ... | | 3,75,000 |
| *7% Mortgage Debenture Sinking Fund | | 1,93,383 |
| *Note.*—Debenture Sinking Fund contributions are in arrears to date by Rs. 75,000 ... | | |
| **Loans Secured :—** | | |
| Imperial Bank of India (Secured on Stock in trade) ... | 14,74,662 | |
| Interest accrued on 7% Mortgage Debenture Bonds ... | 26,250 | |
| | | 15,00,912 |

*Represented by Investment amounting to Rs. 1,84,866

**2. The Titaghur Paper Mills Co., Ltd, B/S. as on 30th September 1942**

| | Rs. a. p. | Rs. a. p. |
|---|---|---|
| **Mortgage Debentures :—** | | |
| Fourth Issue ($4\frac{1}{2}$%) | | |
| Secured on the whole undertaking of the Company *excluding Stocks* and Stores ... | 25,00,000 0 0 | |
| Interest accrued and due | 31,306 8 2 | |
| | | 25,31,306 8 2 |
| *Debentures Redemption Reserve | | 10,00,000 0 0 |

*The Debenture Redemption Reserve is represented by investments on the assets side of the Balance Sheet as follows —

| **Debenture Redemption Fund Investments :—** | Rs. | Rs. |
|---|---|---|
| 5% Loan 1945-55 for Rs. 6,64,000 (at or under market rate) ... | 6,64,000 | |
| $4\frac{1}{2}$% T. P. Mills Debentures for Rs. 3,36,000 | 3,36,000 | 10,00,000 |

This shows that a portion of the redemption fund monies has been used for redeeming the debentures. The debentures so redeemed have not been cancelled, but are kept alive and treated as investments.

3. The Sijna (Jherriah) Electric Supply Co., Ltd. B/S. as on 31st Dec. 1939

| | Rs. | Rs. |
|---|---|---|
| 5 per cent First Mortgage Debentures :— | | |
| 8,000 Debentures of Rs. 500 each issued | 40,00,000 | |
| *Less* 4,731 Debentures of Rs. 500 each redeemed | 23,65,500 | |
| 3,269 | 16,34,500 | |
| *Less* 1,045 Debentures of Rs. 500 each deposited with the Imperial Bank of India as Collateral Security against Cash Credit Account | 5,22,500 | 11,12,000 |
| (Secured against all Land, Buildings, Plant and all Machinery of every kind, all Fixtures, Book and other Debts and uncalled Capital) | | |
| **Loans Secured :—** | | |
| Debenture Interest accrued .. | | 28,000 |

4. **The Associated Cement Co., Ltd.—B/S. on 31st July 1940**

| Previous year Rs | | Rs. | Rs. |
|---|---|---|---|
| | **Loans Secured :** | | |
| | *(a)* 5½% Mortgage Debenture Bonds (Secured by charge on Fixed Assets of the Wah Works) | | |
| 5,00,000 | As per last Account | 4,05,000 | |
| 95,000 | *Less*—Redeemed during the year | 1,00,000 | 3,05,000 |
| 4,05,000 | *(b)* Amount drawn against Cash Credit with Imperial Bank of India (Secured by hypothecation of Stocks of cement, clinker, coal, bags, gypsum and limestone at the factories of the Company) | | 18,62,548 |

5. **The Tata Hydro-Electric Power Supply Co. Ltd., B/S. on 30th June 1940**

| As at 30-6-39 Rs. | | Rs. | Rs. |
|---|---|---|---|
| 1,16,89,100 | 6% Mortgage Debentores (1941) | 1,16,89,100 | |
| | *Less*—Purchased and cancelled | 1,40,000 | 1,15,49,100 |
| | (The security constitutes a First Charge on immovable property, plant and license of the Company and a floating charge on all other assets and a fixed charge on the 'C' Debentures of the Tata Power Co., Ltd of the nominal value of Rs. 1,00,00 000) | | |
| | **Loans (Secured) :—** | | |
| | Cash credit with Imperial Bank of India, Bombay, for Rs. 10,00,000 (now reduced to Rs. 9,70,000) secured by 5% 1945–55 India Loan of the face value of Rs. 10,00,000 (as per contra) | | |
| Nil | Drawings at date of Account | | Nil |

6. **The Kohinoor Mills Co., Ltd.,—B/S. as on 31st December 1940**

| 1939 Rs. | | Rs. | Rs. |
|---|---|---|---|
| | Mortgage Debenture Loan (Secured by a lien on the fixed assets) $4\frac{1}{2}\%$ redeemable on 1-5-1942 | | |
| 4,55,000 | | 4,55,000 | |
| 3,223 | Interest accruing but not due | 3,223 | 4,58,223 |
| 4,58,223 | **Loan Secured :—** | | |
| 33,496 | Chartered Bank of India, Australia and China (Secured by a lien on the Stocks and Stores) | | 6 29,950 |
| | **Loans Unsecured :—** | | |
| 7,06,973 | Killick, Nixon & Co. Rs. 5,34,000 | | |
| | Interest due but not paid 6,608 | 5,40,608 | |
| 6,86,091 | Fixed Deposits 16,97,217 | | |
| 8,808 | Interest accruing but not due 21,326 | 17,18,543 | 22,59,151 |
| 14,01,872 | | | |

**7. The Indian Iron & Steel Co., Ltd.—B/S. as on 31st March 1940**

| | | | |
|---|---|---|---|
| Schedule "C"—DEBENTURES | | | Rs |
| 4% First Mortgage Debentures · | | | |
| Secured on the immovable properties of the Company including the immovable properties and other assets of The Bengal Iron Co, Ltd. (In Liquidation) transferable in terms of the Scheme of Amalgamation and by a floating charge on the whole of the undertakings and assets of both these Companies | | £1,500,000 | 2,00,00,000 |
| 4% Convertible Second Mortgage Debenture Stock : | | | |
| Secured on the immovable properties of the Company including the immovable properties and other assets of The Bengal Iron Co., Ltd, (In Liquidation) transferable in terms of the Scheme of Amalgamation and by a floating charge on the whole of the undertakings and assets of both these Companies subject to the rights of the 4% First Mortgage Debentures The 4% Convertible Second Mortgage Debenture Stock is convertible at any time up to 31st December, 1943 into Ordinary Shares at the rate of one Ordinary Share of Rs. 10 for each £1-10-0 of Convertible Stock– | | | Rs. |
| Issued ... ... | | £500,000 | |
| Converted before 31 March 1939 | £4,56,990 | | |
| Converted during the year | £2,814 | £459,804 | |
| | | £40,196 | 5,35,946 |
| Deferred Participating Income Debenture : Unsecured | | | |
| In accordance with the Amalgamation agreement, dated the 8th September 1935, with The Bengal Iron Co,, Ltd., this Debenture will be cancelled on completion of the transfer but by arrangement with the Liquidator interest thereon has ceased to run as from the 1st April, 1936 A similar arrangement has been made in respect of the £5,000 Participating Income Debenture of The Bengal Iron Co. Ltd. (In Liquidation) held as per contra | | | 75,000 |
| | | | 2,06,10,946 |

### 4. Current Liabilities.

The debentures and loans of a company are its term liabilities—either long-term or short-term. Besides these, every company has other liabilities which are payable without any limit of time, and these are called current liabilities. Form F requires that these liabilities are shown as follows :—

Liabilities :—

For Goods supplied
For Expenses
For Acceptances
For Other Finance

This classification of current liabilities is intended to furnish the shareholders with sufficient information regarding the company's immediate commitments.

The item 'For Other Finance' is an omnibus item, which may include liabilities for—

(a) Capital Expenditure ;
(b) Security Deposists ;
(c) Interest outstanding on such deposits ;
(d) Managing Agent's Commission ;
(e) Provision for Taxation ;
(f) Any other specific reserve ;
(g) Staff Bonus ;
(h) Unadjusted Balances ;
(i) Advances against orders, etc.

These items are very often disclosed separately under the heading 'Liabilities' ; but sometimes they are merged in the omnibus item 'Other Finance'.

While secured and unsecured loans from subsidiary companies are required to be given in the balance sheet as distinct items, any trading debts due to subsidiary companies are not to be shown separately.

The following extracts from the actual balance sheets of Indian companies will illustrate how current liabilities are shown :—

**1. The Indian Wood Products Co., Ltd. B/S as on 30th September 1941**

| | Rs. | Rs. |
|---|---|---|
| **Liabilities :—** | | |
| For goods supplied ... | 3,783 | |
| „ Expenses ... | 58,148 | |
| „ General Manager's and Assistants' Commissions ... | 18,569 | |
| „ Commission due to Mg Agents ... | 12,127 | |
| „ Security Deposits ... | 54,789 | |
| „ Interest on Security Deposits ... | 1,248 | |
| „ I. T. and S. T. ... | 1,56,260 | |
| „ E. P. T. ... | 2,56,367 | |
| „ Other Finance ... | 372 | |
| „ Company's contribution to Staff Provident Fund | 2,755 | |
| | | 5,64,418 |

2. The Associated Cement Co., Ltd. B/S. as on 31st July 1940

| | Rs. | Rs |
|---|---|---|
| **Liabilities :—** | | |
| For goods supplied ... | | |
| „ Expenses ... | | |
| „ Other Finance ... | | |
| „ Land and Buildings ... | | |
| „ Sundry Deposits ... | | |
| „ Mg. Agents Commission ... | | |
| „ Amount due on sales of cement made by this Company on behalf of the Patiala Cement Co., Ltd. ... | | |

3. *The Tata Hydro.Electric Power Supply Co., Ltd.* B/S. as on 30th June 1940

| | | |
|---|---|---|
| **Current Liabilities :—** | | |
| For Goods supplied, Work done, etc. | | |
| „ Expenses ... | | |
| „ Bonus to Staff ... | | |
| „ Agents' Commission ... | | |
| „ Amount due to Allied Company :— The Andhra Valley P. S. Co., Ltd. United Power Ltd. ... | | |
| „ Other Finance (including unadjusted balances) ... | | |

4 The Ahmedabad Electricity Co., Ltd. B/S as on 30th September 1940

| | | |
|---|---|---|
| **Liabilities :—** | | |
| Due to Callender's Cable and Construction Co., Ltd. .. | | |
| For Goods supplied .. | | |
| „ Expenses (including Agents' Commission) ... | | |
| „ Service and Security Deposits from Consumers ... | | |
| „ Other Finance ... | | |
| „ Taxation ... | | |

5. The Dunlop Rubber Co. (India) Ltd.—B/S. as on 31st December 1940.

| | | Rs | Rs |
|---|---|---|---|
| **Current Liabilities :—** | | | |
| Sundry Creditors (unsecured) | | | |
| Associated Companies | Rs. 32,821 | | |
| Others | 2,12,294 | 2,45,115 | |
| For Expenses ... ... ... | | 1,70,077 | 4,15,192 |

| | | |
|---|---|---|
| National Bank of India, Ltd. Overdraft on Current Account (secured by guarantee of Dunlop Rubber Co., Ltd.) ... | | 18,97,894 |
| Unclaimed Dividends ... ... | | 4,016 |
| **Proposed Dividends :—** | | |
| Guaranteed Preference Dividend for half year to 31-12-40 (since paid) ... | 90,000 | |
| 2nd Preference Dividend for year to 31-12-40 ... ... ... | 1,90,000 | |
| Ordinary Dividend for year to 31-12-40 ... | 10,00,000 | 12,80,000 |

6. **The Tata Oil Mills Co., Ltd.—B/S. as on 31st March 1941.**

| | Rs. | Rs. |
|---|---|---|
| **Liabilities :—** | | |
| For goods supplied ... ... | 3,15,085 | |
| „ Expenses ... ... ... | 1,58,254 | |
| „ Mg. Agents' Comn. (subject to adjusment) | 29,122 | |
| „ Advance against orders ... ... | 34,034 | |
| „ Other Finance ... ... | 42,386 | |
| „ Security Deposit from agents and others | 3,34,454 | |
| „ Construction of Sewri Factory ... | 32,000 | 9,45,335 |

### 5. Balance of Profit & Loss Account.

The item 'Profit and Loss' (meaning thereby the balance of Profit and Loss Account) appears on both sides of Form F. That is to say, if the profit and loss account shows a credit balance, it will appear on the liabilities side; and if it has a debit balance, it will go on the assets side. Apparently the balance of the profit and loss account which is to be entered in the balance sheet is the balance remaining after giving effect to the various profit appropriations in that account. Some companies, however, do not show the profit appropriations in the profit and loss account, but detail them on the balance sheet, as the following illustration will show.

1. **The Pankaja Mills, Ltd.—B/S. as on 31st December 1943.**

| | | Rs. | Rs. |
|---|---|---|---|
| *Profit and Loss Account :—* | | | |
| Balance as per last Balance Sheet ... | | 13,43,542 | |
| *Less* Appropriations thereof— | | | |
| Provision for Taxes | 10,00,000 | | |
| Transfer to Reserve Account | 1,20,000 | | |
| Transfer to Mortgage Redemption Fund | 65,000 | | |
| Dividends | 1,50,000 | 13 35,000 | |
| | | 8,542 | |
| *Add* Net Profit since last Balance Sheet ... | | 31,72,439 | |
| | | 31,80,981 | |
| *Less* Transfer to Reserve Account | 4,00,000 | | |
| Provision for Taxes | 25,20,000 | 29,20,000 | 2,60,981 |

## 6 Contingent Liabilities.

A contingent liability is a liability which may or may not arise. It is a possible liability · but on the happening of a certain event it may become an actual liability. When a contingent liability materialises it may involve the company in a loss being sustained or it may result in the acquisition of an asset of a corresponding amount.

It is not usual to record contingent liabilities in the books of account; but Form F requires that a reference should be made to them by way of footnotes in the balance sheet. Below are given examples of contingent liabilities :—

1. The Associated Cement Co., Ltd. B S. as on 31st July 1940.

| | Rs. |
|---|---|
| 1. Amount uncalled on 3,610 Shares of the Cement Marketing Co. of India, Ltd., at Rs. 90 per share ... ... | 3,24,900 |
| 2. Amount to be paid contingent on the exercise of options in respect of purchase of lands | 27,000 |

2. The Elgin Mills Co., Ltd. B. S. as on 30th September 1940.
   Drafts discounted by Bank Rs. 3,105.

3. The Delhi Flour Mills Co., Ltd. B. S. as on 31st October 1940.
   On account of 10% commission payable to managing agents on the year's net profits in the event of the declaration of a dividend on the Ordinary Shares of 5% or over Rs. 2,403.

4. The Kumardhubi Engineering Works. Ltd. Balance Sheet as on 30th November 1938.
   Arrears of Dividend on Preference Shares up to 30th November 1937 Rs 14,70,000

5. The Bombay Electric Supply and Tramways Co, Ltd. Balance Sheet as on 31st December 1940.
   Claims against the Company not acknowledged as debts Rs. 2,72,379.

6. The Indian Iron and Steel Co. Ltd. B/S. as on 31st March 1940.
   The Company has unconditionally guaranteed both as to principal and interest £1,000,000 4½% Guaranteed Convertible Mortgage Debentures of the Steel Corporation of Bengal, Ltd. The said guarantee has been secured by a charge upon the assets and undertaking of the Company ranking immediately after the mortgage securing the Company's 4% Convertible Second Mortgage Debenture Stock. Any sums paid under the guarantee are secured by a charge on the undertaking of the Steel Corporation of Bengal, Ltd., ranking immediately after the principal and interest on the said £1 000,000 4½% Guaranteed Convertible Mortgage Debentures.

7. The Samastipur Central Sugar Co., Ltd. Balance Sheet as on 30th June 1940.
   The Indian Sugar Syndicate, Ltd. (*i*) Undertaking to contribute in the event of the Syndicate being wound up, in accordance with the provisions of Clause 5 of the Memorandum of Association; and (*ii*) Liability to contribute, on sugar produced, in accordance with the provisions of Clause 32 (d) of the Articles of Association.

# CHAPTER 3

## THE BALANCE SHEET—(2)

The Liabilities side of a company balance sheet was explained in the preceding chapter. Now we shall take up the assets side of the balance sheet, and the principal items appearing therein will be discussed in detail.

### 1. *Fixed Capital Expenditure.*

Fixed or Capital assets are those assets by means of which the business operations are carried on, and which are held for the purpose of earning income and not for the purpose of resale as, for example, land, buildings, plant and machinery, furniture, motor vehicles, railway siding, etc. It is to be noted that the adjective 'fixed' is used in a relative sense; there must be an element of continuity. It does not mean that the fixed assets must be fixed to the ground.

The successful continuance of a business depends upon the maintenance of its fixed assets. Those fixed assets which, by their nature, are consumed in the service of the business by efflux on of time (such as leases) or by wear and tear (such as machinery) or by consumption (such as mines) are known as *Wasting Assets*

Floating assets, on the other hand, are those that are intended for resale, or which in the ordinary course of business will be converted into other assets, such as stocks, stores, book debts, investments, and cash balances Those floating assets which are in the form of cash and other easily realisable form are called *liquid assets.*

Assets which would be fixed assets in one business may be floating assets in another, the determining factor being the intention with which an asset is held, e. g., furniture in the case of a hotel is a fixed asset while furniture in the case of a furniture dealer is a floating asset.

In Indian accountancy practice, the usual collective name for the fixed assets of a business is '*Block Account*' or simply '*Block*'. The various fixed assets stated at their original cost are referred to as '*Total Block Expenditure*' or '*Gross Block Expenditure*' or '*Total Block Account*' or simply '*Total Block*' or '*Gross Block*'. On the other hand the term '*Net Block*' or '*Depreciated Block*' or '*Net Depreciated Block*' means the original cost minus the total depreciation provided since the various fixed assets were acquired.

The fixed assets of a business are also known as capital assets or capital expenditure. In Form F the term used for the fixed assets or capital expenditure is 'Fixed Capital Expenditure'. The use of both the words 'fixed' and 'capital' is therefore for the sake of emphasis

**Requirements of Form F with regard to Fixed Assets.** The following information relating to the fixed assets of a company is to be given in its balance sheet :—

Fixed Capital Expenditure—

(Distinguishing as far as possible between expenditure upon goodwill, land, buildings, leaseholds, railway sidings, plant, machinery, furniture, development of property, patents, trade marks and designs, interest paid out of capital during construction etc., and stating in every case the original cost and the additions thereto and the deductions therefrom during the year, and the total depreciation written off under each head. Where sums have been written off on a reduction of capital or a revaluation of assets, every balance sheet after the first balance sheet subsequent to the reduction or revaluation shall show the reduced figures with the date of and the amount of the reduction made).

Preliminary Expenses

Commission or Brokerage

(Commission or Brokerage paid for underwriting or placing or subscribing shares or debentures until written off).

Discount allowed on the issue of shares or so much as has not been written off at the date of the balance sheet.

Live-stock and Vehicles

The above requirements of law with regard to the fixed assets of a company may be analysed as follows :—

1. As far as possible, the various fixed assets (such as goodwill, land, buildings, leaseholds, railway sidings, plant, machinery, furniture development of property, patents, trade marks and designs, interest paid out of capital during construction, etc.) are to be given separately. The words as far as possible' are intended for those rare cases where, for want of information, this requirement cannot be complied with.

2. In every case (i. e., in the case of each fixed asset) the original cost and the additions thereto and deductions therefrom made during the year must be stated.

The 'original cost' means the original cost of the existing assets as at the beginning of the year.

The 'additions' made during the year may include *(a)* the cost of actual additions ; *(b)* the amount added on reorganisation of capital or revaluation of assets : or *(c)* the cost of items transferred from other assets.

The 'deductions' made during the year may be on account of

*(a)* The cost of items sold ;

*(b)* The cost of items transferred to other assets ;

*(c)* The cost of items eliminated where such items have been entirely used up or where they are scrapped or discarded;

*(d)* The amount transferred from a special reserve, e. g., Block Improvement Reserve or Property Reserve ;

(e) The amount actually written off on reduction of capital or revaluation of assets made during the year.

A few companies, besides showing the amount of deductions made during the year, also give all previous years' deductions, although such a disclosure is not required by law. Here is an example from the published balance sheet of the British India Corporation, Ltd., as on 31st December 1943:

| | Rs. | Rs. |
|---|---|---|
| Plant and Machinery : | | |
| Cost to 31st December 1942 | 1,97,65,116 | |
| Additions during the year | 4,63,934 | 2,02,29,050 |
| *Less* Sales to 31st December 1942 | 1,23 546 | |
| Sales during the year | 3,900 | 1,27,446 |
| | | 2,01,01,604 |

In this case the original cost of Plant and Machinery as on 1st January 1943 (Rs. 1,97,65,116) is not the cost of the asset in existence on that date but it is the cost of the entire asset acquired from the beginning. That is not the requirement of the law. This asset should therefore be shown as follows:—

| | Rs |
|---|---|
| Plant and Machinery : | |
| Cost to 31st December 1942 | 1,96,41,570 |
| Additions during the year | 4,63,934 |
| | 2,01,05,504 |
| *Less* Sales during the year | 3,900 |
| | 2,01,01,604 |

3. Where any amounts have been written off fixed assets on a reduction of capital or revaluation of assets, it is necessary to show (*i*) the reduced figure, (*ii*) the date of reduction, and (*iii*) the amount of reduction in every balance sheet after the first balance sheet subsequent to the reduction or revaluation.

This requirement does not apply to the first balance sheet subsequent to the reduction or revaluation, because such particulars would necessarily be given in that balance sheet on account of deductions made during the year.

This information may be given in one of the following two ways:

**Balance Sheet as on 31st December 1945**

| | Rs. | Rs. |
|---|---|---|
| Plant and Machinery : | | |
| Original cost to 31st December 1944 (after writing off Rs. 1,00,000 on Reduction of Capital in May 1932) | | 3,45,000 |
| *Or,* | | |
| Plant and Machinery : | | |
| Original cost to 31st December 1944 | 4,45,000 | |
| *Less* Written off on Reduction of Capital in May 1932 | 1,00,000 | 3,45,000 |

4. While the law provides for the disclosure of amounts written off fixed assets on a reduction of capital or revaluation of assets, there

is no provision as to how an increase in the value of fixed assets on a revaluation is to be shown. Apparently it is to be dealt with in the same way as a reduction, e. g., the landed property appeared as follows in the balance sheet of the Champarun Sugar Co., Ltd., as on 30th June 1942 :—

| | Rs. | Rs. | Rs. |
|---|---|---|---|
| Landed Property : | | | |
| Cost as at 30th June 1941 ... | 1,95,706 | | |
| *Add* Surplus on revaluation in 1928 | 4,93,788 | | |
| | 6,89,494 | | |
| *Less* Sales and adjustments to 30th June 1941 ... | 3,12.288 | 3,77,206 | |
| Added during the year ... | | 187 | |
| | | 3,77,393 | |
| *Less* Sales during the year ... | | 515 | 3,76,878 |

It must be noted that in this case the previous years' deductions are also given ; and therefore the original cost as at the beginning of the year (i. e , on 1st July 1941) is that of the entire land purchased by the Company and not only that of the land actually in existence on that date.

5. In the case of interest paid out of capital during construction under section 107, which is debited to Block Account, the capital on which and the rate at which such interest is paid are also to be stated in the balance sheet.

6 For each fixed asset the total amount of depreciation written off up to the date of the balance sheet is to be shown by way of deduction from its original cost. The law does not require that depreciation written off up to the end of the previous year and that written off for the year should be given separately ; but this is usually done in practice.

The amount of depreciation applicable to items sold, eliminated or transferred during the year is to be deducted from the total depreciation provided in respect of those items up to the beginning of the year.

When depreciation on block is provided for by means of a Depreciation Fund, no depreciation can be shown on the assets side of the balance sheet under each fixed asset, but a note like the following is made on the assets side : 'Depreciation as per Contra' or 'Against the Total Capital Expenditure of Rs. ..........there stands to the credit of the Depreciation Fund Account Rs............'.

7. If on the date of the balance sheet there is any capital expenditure which cannot be allocated to different fixed assets, then it can be shown under any of the following heads : Capital Suspense · Block Suspense ; Capital, Work-in-Progress , Unallocated Expenditure on New works , New Factory under Construction.

8 In Form F 'Live-stock and Vehicles' (a fixed asset) appears separately from Fixed Capital Expenditure and no mode of valuation is required in respect thereof. But according to section 132 (1) the balance sheet should disclose how the value of the fixed assets has been arrived at. Therefore it is necessary that the mode of valuation of Livestock and Vehicles should also be stated in the balance sheet. In practice this is usually done, since this particular fixed asset is treated as a part of the Block Account.

9. Since Form F requires a large amount of information relating to the fixed capital expenditure of a company to be disclosed in its balance sheet, many companies are now adopting the practice of using separate schedules for the purpose. These schedules are to be attached to and to form part of the balance sheet.

The following illustrations taken from the published accounts of Indian companies will show how the Block Account is shown in the balance sheets :—

**1. The Tide Water Oil Co. (India) Ltd.— B/S. as on 30th April 1940**

| | Rs. | Rs. | Rs. |
|---|---|---|---|
| **Motor and other Vehicles—** | | | |
| As per last Account at cost | 35,448 | | |
| Added this half-year | 4,150 | | |
| | 39,598 | | |
| *Less* Original cost of vehicles sold | 6 725 | 32,873 | |
| *Less* Depreciation as per last Account | 13,540 | | |
| Added this half year | 4,465 | | |
| | 18,005 | | |
| *Less* Depreciation provided on vehicles sold | 2,513 | 15,492 | 17,381 |

**2. The Muir Mills Co., Ltd.— B/S. as on 31st December 1940**

| | Rs. | Rs. |
|---|---|---|
| **Buildings—** | | |
| Cost to 31-12-1939 | 21,16,533 | |
| Added during the year | 22,866 | |
| | 21,39,399 | |
| *Less* Depreciation written off to date | 11,45,047 | 9,94,352 |

*Note*—The depreciation written off to 31 12 1939 and the depreciation written off for 1940 are merged together.

3. *The Saran Engineering Co., Ltd B/S, as on 31st March 1940*

| | Rs. | Rs. | Rs. |
|---|---|---|---|
| **Conveyances :—** | | | |
| At cost as at 31-3-1939 ... | 7,873 | | |
| Added during the year ... | 4,950 | | |
| | 12,823 | | |
| *Less* Sale and adjustment | 4,576 | 8,247 | |
| *Less* Depreciation to 31-3-1939 .. | 7,373 | | |
| Provision for the year | 1,400 | | |
| | 8,773 | | |
| *Less* Adjustment* ... | 3 576 | 5,197 | 3,050 |

*This is in respect of the item sold during the year.

4. **The Gold Mohur Mills, Ltd B/S. as on 31st December 1940**

| 1939 Rs. | | Rs. | Rs. |
|---|---|---|---|
| | **Plant and Machinery —** | | |
| | Cost to 31-12-1939 ... | 39,32,852 | |
| | Additions this year ... | 50,718 | |
| | | 39,83,570 | |
| | *Less* Sales* ... | 33,940 | |
| | | 39,49,630 | |
| | *Less* Transferred to "Loss on Sale of Machinery* | 6,17 165 | |
| | | 33,32,465 | |
| | *Less* Depreciation written off in previous years 1,20,000 | | |
| | *Less* Proportionate Depreciation on machinery sold 22,925 | | |
| 38,12,852 | | 97,075 | 32,35,390 |
| | Loss on Sale of Machinery :— | | |
| | Loss as above 6,17,165 | | |
| | *Less Proportionate* Depreciation 22,925 | 5,94,240 | |
| | *Less* Written off this year | 1,20,655 | 4,73,585 |

*These two could have been combined as either "Sale and adjustment" or "Cost of machinery sold."

**5. The Hingir-Rampur Coal Co., Ltd. B/S. as on 30th June 1940**

| | | Rs. | Rs. |
|---|---|---|---|
| Machinery and Plant :— | | | |
| Total cost to 30-6-1939 (after writing off Rs. 30,150 on Reduction of Capital on 4-9-1915) ... | | 2,77,382 | |
| *Less* Deductions during the year ... | | 11,644 | |
| | | 2,65,738 | |
| Additions during the year — | | 17,854 | |
| | | 2,83,592 | |
| *Less* Depreciation written off to 30-6-1939 | 2,63,047 | | |
| *Less* Deductions | 9 945 | | |
| | 2,53,102 | | |
| Written off during the year | 4 620 | 2,57,722 | 25,870 |

**6. The Saran Engineering Co., Ltd. B/S. as on 31st March 1940**

| | Rs. | Rs. |
|---|---|---|
| Patterns :—At cost as at 31-3-1939 ... | 4,013 | |
| *Less* Depreciation to 31-3-1930 | 4,013 | |

*Note.*—The asset is still in existence, although it has been completely depreciated.

**7. The Sijna (Jherriah) Electric Supply Co., Ltd.**
**B/S. as on 31st December 1939**

| | Rs. | Rs. | Rs. |
|---|---|---|---|
| Motor Cars :— | | | |
| Original Cost as per last Account ... | 19,234 | | |
| *Less* Elimination of items not represented by Assets ... | 12,074 | 7,160 | |
| *Less* Total Depreciation as per last Account | 17,234 | | |
| *Less* Depreciation on eliminated Items ... | 12,074 | | |
| | 5,160 | | |
| Depreciation since added | 1,000 | 6,160 | 1,000 |

8. The Burrakur Coal Co., Ltd. B/S. as on 31st December 1940

| | Rs. | a. | p. | Rs. | a | p | Rs | a. | p. |
|---|---|---|---|---|---|---|---|---|---|
| *Machinery and Plant :—* | | | | | | | | | |
| Expenditure to 30-6-1940 ... | 89,60,235 | 8 | 2 | | | | | | |
| Since added ... | 19,751 | 3 | 7 | | | | | | |
| | 89,79,986 | 11 | 9 | | | | | | |
| *Less* Sold ... | 2,000 | 0 | 0 | 89,77,986 | 11 | 9 | | | |
| *Less* Depreciation to 30-6-1940 | 62,13,235 | 8 | 2 | | | | | | |
| Since added ... | 30,751 | 3 | 7 | 62,43,986 | 11 | 9 | 27,34,000 | 0 | 0 |
| *Note,* The total expenditure on Fixed Assets has been reduced by the elimination of the value of items which are no longer existent or have no value, and Depreciation has also been reduced by the relative amount as follows :— | | | | | | | | | |
| Machinery and Plant | | | | 5,26,901 | 0 | 0 | | | |

9. The Tata Oil Mills Co., Ltd. B/S. as on 31st March 1941

| | Rs. | Rs. |
|---|---|---|
| **Buildings at Tatapuram and Sewri :—** | | |
| Cost to 31st July 1928 ... | 13,86,812 | |
| *Less* Written off under Scheme of Arrangement on *31st July 1928* | 1,86,812 | |
| Balance as on 1st August 1928 ... | 12,00,000 | |
| Additions *less* adjustments and deductions up to 31st March 1940 ... | 4,58,932 | |
| Balance on 31st March 1940 ... | 16,58,932 | |
| Additions this year Rs. 42,372 *less* deductions this year Rs. 3,186 ... | 39,186 | 16,98,118 |

*Note.* The Depreciation has been provided for by means of a "Depreciation Fund" which on this date amounts to Rs. 8,36,666 against the gross Block of Rs. 54,69,119. The provision for depreciation is in the Directors' opinion still inadequate.

This can be better shown as follows :—

| | Rs | Rs. |
|---|---|---|
| **Buildings at Tatapuram and Sewri :—** | | |
| Cost to 31st March 1940 ... | 18,45,744 | |
| *Less* Written off under Scheme of Arrangement on 31-7-1928 | 1,86,812 | |
| | 16,58,932 | |
| Additions during the year ... | 42,372 | |
| | 17,01,304 | |
| *Less* Deductions during the year ... | 3,186 | 16,98,118 |

10. **The Titaghur Paper Mills Co , Ltd.,**

| Name | Cost at<br>-<br>30—9—40 | | | Amount added on Reorganisation of Capital as per resolution dated 7—8—37 | | | Amount added during the half-year ended 31—3—41 | | | Amount deducted or sold during the half year ended 31—3—41 | | | Amount written off under High Court order dated 23—7—25 | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Rs. | a | p | Rs. | a. | p. | Rs. | a. | p. | Rs. | a. | p | Rs. | a. | p. |
| Land and Buildings | 33 62,629 | 2 | 10 | 2,50,000 | - | - | 40 279 | 12 | 10 | - | - | - | 30,000 | | - |

*Note.* The law does not expressly require that any amounts added to fixed should be shown separately in every subsequent balance sheet. off fixed assets on account of reduction of capital or revaluation of

11, **The Indian Iron & Steel Co , Ltd.,**
**Schedul "D" Fixed**

| | Col I | Col II | Col III | Col IV | Col V |
|---|---|---|---|---|---|
| | Original cost to 31st March 1939 | Additions for year to 31st March 1940 | Deductions for year to 31st March 1940 | Amount written off by order of High Court dated 12th June 1925 | Amount written off by order of High Court dated 25th Nov. 1936 |
| | Rs | Rs. | Rs. | Rs. | Rs. |
| Land . | 2,72,292 | 21 003 | – | – | – |
| Buildings .. | 55,00,720 | 9,03,177 | 3 744 | 8 28,486 | 4,78,664 |
| Roads and Drains . | 4,10,231 | 37,030 | – | 1,85,473 | 50,000 |
| Mining Properties .. | 32 72,022 | – | 3,95,603 | 8,57,614 | 3,03,018 |
| Railway Sidings | 15,81,089 | 30,300 | – | 3,77,534 | 1,25,000 |
| Plant and Machinery .. | 3,30,24,728 | 31,49,410 | 1,09,645 | 1,12,18,439 | 26,31,518 |
| Development | 3,73,564 | – | 1,17,712 | 2,55,328 | 524 |
| Furniture . | 3,66,886 | 25,067 | 2,230 | 1,12,977 | 8,500 |
| Total Rs | 4,48,01,532 | 41,65,987 | *6 28,934 | 1 38 45,851 | 35,97,224 |

*Includes Depreciation of Rs. 3,57, 784 provided in past year's accounts

*Note.* The item "Development" though completely written off, will have In the next balance sheets on 31st march 1941, the total of arrived at as shown below :—

**Schedule of Fixed Capital Expenditure as on 31st March 1941.**

| Total | | | Total Depreciation to 30–9–40 | | | Depreciation added during the half year ended 31–3–41 | | | Total Depreciation | | | Net value of Assets as per Balance Sheet | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Rs. | a. | p. | Rs | a | p | Rs. | a. | p | Rs | a | p | Rs. | a. | p |
| 36,22,908 | 15 | 8 | 22,62,629 | 2 | 10 | 60,279 | 12 | 10 | 23,22,908 | 15 | 8 | 13,00 000 | – | – |

capital expenditure on revaluation of assets or reorganisation of capital But it is a good thing to do so in view of the fact that the amounts written assets have to be showo in every subsequent balance sheet.

**B/S. as on 31st March 1940.**
**Capital Expenditure.**

| Col VI | Col VII | Col VIII | Col IX | Col X | Col XL |
|---|---|---|---|---|---|
| Total | Depreciation written off to 31st March 1939 | *Less* Depreciation included io Col III | Depreciation written off for year to 31st March 1940 | Total Depreciation written off | Balance as at 31st March 1940 |
| Rs. | Rs | Rs. | Rs. | Rs. | Rs. |
| 2,93,295 | – | – | – | – | 2,93,295 |
| 50 93,003 | 10,08,570 | 173 | 76,606 | 10,85,003 | 40,08,000 |
| 2,11,788 | 758 | – | 1 030 | 1,788 | 2,10,000 |
| 17,15,787 | 3,36,390 | 2,36,390 | 17,787 | 1,17,787 | 15,98,000 |
| 11,08,855 | 2,88 555 | – | 10,300 | 2,98,855 | 8,10,000 |
| 2,22,14,536 | 69,13,770 | 3,509 | 5,68,073 | 74,78,334 | 1,47,36,202 |
| – | 1,17 712 | 1 17,712 | – | – | – |
| 2,68 246 | 1,65,409 | – | 12,837 | 1,78,246 | 90,000 |
| 3,09,05,510 | 88,31,164 | 3,57,784 | 6 86,633 | 91,60,013 | 2,17,45,497 |

and adjusted as per column VIII.

to be shown in every subsequent balance sheet as required by form F.
Column I headed "Original Cost to 31st March 1940" will be Rs. 4,83,38,585

| | | Rs. |
|---|---|---|
| Net Block on 31-3-1940 | | 2,17,45,497 |
| Total depreciation written off to that date | ... ... ... | 91,60,013 |
| Amount written off by a Court order dated 12-6-1925 | ... ... | 1,38,35,851 |
| Amount written off by a Court order dated 26-11-1936 | ... ... | 35,97,224 |
| Original cost as on 31-3-1940 | ... ... ... | 4,83,38,585 |

12.

**The Ahmedabad Electricity Co., Ltd.—B/S as on 30th September 1940**

Schedule "A"—Fixed Capital Expenditure

| | Costs | | | | | Depreciation written off | | | | | Net |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | As at 30th Sept. 1939 | Additions during 1939-40 | Sub-Total | Deductions during 1939-40 (sales etc.) | Gross Block as at 30-9-40 | As at 30th Sept. 1939 | Deduction | Sub-Total | From the Profits of 1939-40 | Total Depreciation Amount | Depreciated Block as at 30-9-40 |
| | Rs. | Rs | Rs | Rs. | Rs | Rs | Rs. | Rs. | Rs. | Rs | Rs |
| Motor Cars & other vehicles | 23,292 | 5,362 | 28,654 | 3 697 | 24,957 | 15,089 | 2,288 | 12,801 | 2,975 | 15,776 | 9,181 |

13.

**The Searsole Coal Co., Ltd.**

Schedule—Analysis of Capital Expenditure as on 31st January 1941

| | Gross Expenditure | | | Depreciation | | | Amount written off under Capital reduction dated 13-8-1934 | Total | Net as per Balance Sheet |
|---|---|---|---|---|---|---|---|---|---|
| | To 31-1-1940 | Added during the year | Total | To 31-1-40 | Added during the year | To 31-1-1941 | | | |
| | Rs. | Rs. | Rs. | Rs. | Rs. | Rs. | Rs | Rs. | Rs |
| Block | | | | | | | | | |
| Machinery and Plant | | | | | | | | | |
| Development | | | | | | | | | |
| Buildings | | | | | | | | | |
| Furniture | | | | | | | | | |
| Railway Siding | | | | | | | | | |
| Electric Installation | | | | | | | | | |

*Note.*—Here the term "Block" stands only for "Collieries and Properties" It does not include all fixed assets.

**Nature of Fixed Assets.** The various fixed assets found in the balance sheets of companies engaged in different trades and indostries may be as follows :—

1. **The Agarpara Co., Ltd. (Jute).** Land ; Buildings ; Machinery ; Electric Installation ; Railway Siding ; Fire Appliances ; Sprinklers Iostallation ; Furnitore ; Motor Lorry ; Jetty.

2. **The Hooghly Mills Co., Ltd. (Jute).** Land ; Buildings ; Machinery ; Furniture ; Jetty and Tramways ; Hydrant Installation ; Sprinkler Service ; Latrines ; Motor Car.

3 **The Borrea Coal Co., Ltd.** Block (representing Collieries); Buildings ; Machinery ; Electric Installation ; Railway) Siding ; Furnitnre.

4. **The Burrakur Coal Co., Ltd.** Collieries and Properties ; Machinery and Plant ; Boildings , Rolling Stock and Tramway ; Pit Sinking and Development ; Siding Construction ; Furniture ; Motor Cars.

5. **The Betjan Tea Co., Ltd.** Land ; Buildings ; Roads and Bridges ; Machinery ; Development.

6. **The Loobah Co., Ltd. (Tea)** Property ; Machinery ; Factory and Buildings ; Bridges ; Tramway ; Motor Trucks ; Motor Boat.

7. **The Champarun Sugar Co , Ltd.** Landed Property ; Buildings; Laboratory ; Machinery ; Electric Installation ; Railway Sidings ; Tramways ; Furuiture Vehicles and Tractors.

8. **The Titaghur Paper Mills Co., Ltd.** Land and Buildings ; Machinery and Plant ; Railway Siding ; Grass Block ; Bamboo Forest Block ; Furnitore ; Flotilla ; Motor Cars ; Motor Lorries.

9. **The Associated Cement Companies Ltd.** Goodwill and Purchase of Rights ; Land ; Buildings ; Machinery, Plant and Kilns ; Roads, Bridges and Fences ; Water Works ; Motor Cars, Trucks, etc.; Electric Installation.

10. **The Tata Oil Mills Co., Ltd.** Land ; Boildings ; Machinery ; Storage Tanks and Pipe Lines ; Boat Basin, Dry Docks, Sea Walls, Railway Sidings, etc.; Furniture, Fixtores and Office Eqnipment ; Motor Launch, Motor Cars, Lorries, Hand Carts Cycles, etc.

11. **The Saran Engineering Co., Ltd.** Boildings ; Machinery ; Forniture ; Railway Siding ; Conveyances ; Patterns.

12. **The Kumardhubi Engineering Works, Ltd.** Leasehold Land ; Stores and Workshop Site ; Machinery and Plant , Boildings; Ramways; Rolling Stock ; Siding and Wharf ; Furniture ; Typewriting and Calculating Machines ; Water Supply Scheme ; Electric Plant ; Transmission Line ; Power Station and Sub-Station Boildings ; Workshop Electric Plant ; Motor Cars ; Motor Lorry.

13 **The Central India S. W. & M. Co., Ltd. (Cotton Textile).** Land ; Buildings ; Officers Quarters and Employees' Chawls ; Machinery and Plant ; Electrical Machinery, etc ; Overhead Cables ; Undergronnd Cables : Dyeing and Bleaching Machinery ; Printing Machinery; Sewage Plant ; Furnitore, Conveyances, etc. ; Electric Fans, Fittings and Fixtures ; Motor Lorries

14. **The New City of Bombay Manufacturing Co, Ltd. (Cotton Textile).** Freehold Land ; Buildings ; Spinning Machinery ; Weaving

Machinery ; Sprinkler Installation ; Humidifier installation ; Electric Light Installation ; Fire Service Installation ; Hydro-Electric Machinery Furniture.

15 **The Cuttack Electric Supply Co , Ltd.** Buildings ; Machinery; Mains ; Public Lamps ; Meters, Indicators and Measuring Instruments; Oil Store Tank ; Furniture and Fittings ; House Services ; Loose and Fixed Tools ; Motor Car and Cycles.

16. **The Sijua (Jherriah) Electric Supply Co., Ltd.** Leasehold Land · Buildings ; Machinery and Plant ; Main Gas Pipe ; Siding ; Mains Transmission Line ; Transmission Line Underground ; River Dams and Silt Wall ; Furniture ; Pipe Line and Water Supply ; Motor Cars ; Motor Lorry

17. **The Guntur Power & Light, Ltd.** Lands ; Buildings ; Plant ; Overhead Mains ; Underground Cables ; Service Connections and Meters ; Transformers ; Eletcric Testing Instruments ; Motor Cars and Lorry ; Pumping Sets and Motors for Hire ; Furniture and Fittings ; Telephone Equipment ; Work in Progress on Extensions ; Refrigerator; Engineering and Development Charges.

18. **The Moradabad Water Supply Co , Ltd.** Pipe Lines, Fittings and Stand posts; Tube Wells; Buildings ; Pumping Plant and Machinery; Elevated Tank and Pipe Connections ; Electric Installation ; Water Meters ; Furniture, Fixtures and Office Equipment ; Acquisition of License ; Preliminary Expenses ; Commission and Brokerage ; Hire-Purchase Installations.

19. **The Bukhtiarpur-Bihar Light Railway Co., Ltd.** Land ; Ballast and Permanent Way ; Bridgework ; Stations and Buildings ; Plant ; Rolling Stock ; Capital Suspense.

20. **The Assam Saw Mills and Timber Co., Ltd.** Leasehold Land; Machinery and Plant ; Pucca Buildings ; Kutcha Buildings ; Tramways; Motor Boat and Launches ; Country Boat ; Motor Lorry ; Motor Tractors and Trailors ; Furniture.

21 **The Indian Wood Products Co., Ltd.** Forest Concession ; Land ; Buildings ; Railway Siding ; Machinery and Plant ; Laboratory Apparatus , Electric Installation ; Furniture ; Patent and Trade Mark Rights ; Motor Car.

22. **The Tata Iron & Steel Co., Ltd.** Mining Rights and Concessions ; Ore Mines and Quarries ; Miscellaneous Properties ; Jamshedpur Land (freehold) and Town Roads ; Town Buildings ; Town Sanitary and Water Works ; Electric Light and Fan Installation ; Water System and Sanitation ; Office and Administrative Buildings ; Technical Institute Building and Equipment ; Works including Mills, Plant, Machinery, etc. ; Implements and Tools Manufacturing Plant ; Chemicals Manufacturing Plant ; Furniture ; Collieries.

## 2. Stores and Spare Parts.

Form F requires that 'Stores and Spare Parts' should appear as a separate asset on the balance sheet. This is an asset which is found in the balance sheets of all mill companies. It may consist of mill stores (lubricants, belting, etc.), spare parts of machinery, unissued machinery, coal, liquid fuel or oil, packing and advertising materials, chemicals, medicines, stationery, loose tools, food grains, etc. Some

of these items, e. g., coal, liquid fuel unissued machinery, loose tools, etc. are often shown as separate assets.

It is not necessary to state in the balance sheet the mode of valuation of stores and spare parts. But this floating asset is generally valued at cost or at under cost, and this fact is indicated in the balance sheet.

In a few companies stores are not shown as a separate asset as they are coupled with stocks; but this treatment does not appear to be strictly in conformity with the law. Here are a few examples showing how this asset actually appears in the published accounts:—

**1. The Dalhousie Jute Co., Ltd. B/S. as on 31st March 1941**

| | | | Rs. |
|---|---|---|---|
| Stores and Spare Gear | ... | ... | 3,02,565 |
| Oil and Coal | ... | ... | 39,978 |

**2. The Burraken Coal Co., Ltd. B/S. as on 31st December 1940.**

| | | | Rs. |
|---|---|---|---|
| Stores and Spare Plant | ... | ... | 5,33,518 |

**3. The Bengal Paper Mill Co., Ltd. B/S. as on 31st December 1940.**

| | Rs. | Rs. |
|---|---|---|
| **Stocks :—** | | |
| Paper, etc. at manufactnred price or nnder | 97,137 | |
| Paper-making materials and stores at nnder cost price ... | 11,08 315 | 12,05,452 |

**4. The Indian Wood Products Co., Ltd., B/S. as on 30th September 1941**

| | | | Rs. |
|---|---|---|---|
| Stores and Tools | .. | ... | 35,315 |

**5. The associated Cement Co., Ltd. B/S. as on 31st July 1940.**

| | Rs. | Rs. |
|---|---|---|
| **Stores, Spare Parts, etc.—** | | |
| On hand (at or below cost-as per inventories certified by the Work Managers) ... | 55,85,474 | |
| In transit (at cost—as certified by the Managing Agents) ... ... | 60,497 | 56,45,971 |
| **Coal, Bags, Gypsum, Limestone and other Raw Materials (at cost)—** | | |
| On hand (as per inventories certified by the Works Managers) ... ... | 81,78,846 | |
| In transit (as certified by the Mg. Agents) ... | 1,73,700 | |
| Bags stored with suppliers ... | 3,14,388 | 86,66,934 |

**6. The Kohinoor Mills Co., Ltd. B/S. as on 31st December 1940.**

| | Rs. | Rs. |
|---|---|---|
| Stores (as per Agents certified inventories) | 6,42,556 | |
| Coal Liqnid Fuel, Grain and Hardware Stores (as per agents certified inventories) | 1,40,260 | 7,82,816 |

**7. The Swan Mills, Ltd. B/S. as on 31st December 1940.**

| | | Rs. |
|---|---|---|
| **Stores and Spares :—** | | |
| At cost as per inventories certified by the Agents— (Qnantities certified by the anditors) | ... | 5,65,772 |

### 3. Stock-in-Trade.

Form F requires that stock-in-trade mnst appear in the balance together its mode of valuation which may be cost or market value. But it mnst be noted that stock in trade may be valued at cost or market value or in any other manner. In fact the various components of stock in trade are in practice valued by Indian companies in the following ways:—at cost; at average cost; at below cost; at market value; at under market value; at sale price; at contract rates; at control ratea

It is not legally necessary to show the various kinds of stock (such as raw materials, work-in-process, finished goods, goods in transit, goods with agents, etc.) separately. They may be all lumped together. But most companies show the different kinds of stocks separately, although the stock in process or stock of partly manufactured goods is in almost all cases put together with the stock of raw materials.

The following extracts illustrate how this asset is shown in the balance sheets :—

**1. The Elgin Mills Co. Ltd. B/S. as on 30th September 1940.**

| | Rs. | Rs. |
|---|---|---|
| **Stock-in-Trade** (Raw materials at cost and manufactured goods at or under market value | | |
| At Mill .. | 28,89,704 | |
| At Depots ... | 13,641 | 29,03,345 |

**2. The Dalhousie Jute Co., Ltd. B/S as on 31st March 1941**

| | Rs. | Rs. |
|---|---|---|
| **Stock in Trade :—** | | |
| Jute at or under cost price ... | 11,59,981 | |
| Cloth and Bags at contract rates | 9,02,536 | 20,62,517 |

**3. The Betjan Tea Co., Ltd. B/S. as on 31st December 1940**

| | Rs. | Rs |
|---|---|---|
| Stock of Tea—Since sold (taken at sale price) ... | 1,25,694 | |
| At valuation (below current market rates) ... | 3,300 | 1,28,994 |

**4. The British India Corporation, Ltd B/S. as on 31st December 1940**

| | |
|---|---|
| **Stock-in Trade** (at or under cost or market value which ever is the lower) ... | Rs. 86 64,097 |

**5. The Tata Oil Mills Co , Ltd. B/S. as on 31st March 1941**

| | | |
|---|---|---|
| **Stocks** (including stocks in transit as certified and valued by the Managing Agents) | Rs. | Rs. |
| Raw Materials and Stocks in Process at cost ... .. | 7,24,065 | |
| Finished Products at below market rates | 7 68,333 | 14 92,398 |

**6 The Brushware, Ltd.,—B/S. as on 30th November 1940**

| | |
|---|---|
| **Stock in-trade :—** | Rs. |
| Manufactured and unmanufactured Brushes and Indian Bristle at cost or market value ... | 1,48,722 |

**7. The Tide Water Oil Co., (India) Ltd., B/S. as on 30th April 1940**

| | | |
|---|---|---|
| **Stocks at or under cost :—** | Rs. | Rs. |
| Landed ... | 10,08,580 | |
| In transit ... | 28,378 | 10,36,958 |

**8 The Kumardhubi Engineering Works, Ltd , B/S. as on 30th November 1941**

| | | |
|---|---|---|
| ***Stock in Trade*** | ***Rs*** | ***Rs.*** |
| Stocks and General Stores at or market cost | 7,45,195 | |
| Work in Progress at or under cost | 24,95,672 | |
| Stores in transit at cost ... | 2,94,659 | 35,35,527 |

**9. The Delhi Cloth & General Mills Co., Ltd B/S as on 30th June 1940**

| | | |
|---|---|---|
| **Stocks on hand (as certified by the Agents)** | Rs. | Rs. |
| Manufactured goods (cloth and yarn) below cost ... | 34,90,363 | |
| Manufactured goods (Tents) at contract rates | 1,37,193 | |
| " (Sugar) below market rate ... | 22,99,280 | |
| Raw Materials (Cotton and tents) at or below cost ... | 44,06,893 | |
| Stock in process (Cloth, yarn and cotton) below cost .. | 4,25,666 | |
| Stock in process (Tents) at contracts rates | 2,14,818 | |
| Stores, coal, gunney bags, etc., at or below cost ... | 9 93 977 | |
| Molasses at market rate ... | 8,906 | 1,19,79,096 |

**10. The Finlay Mills, Ltd B/S. as on 31st December 1940**

| | Rs. | Rs. |
|---|---|---|
| **Stock in Trade :—** | | |
| As per inventories certified by the Agents—(Quantities certified by the Auditors) | | |
| Cotton, in bales on hand, at cost ; in process, at market value ... | 10,45,497 | |
| Yarn, sold, at contract value unsold, at market value ... | 3,33,287 | |
| Waste, sold, at contract value ; unsold at market value ... | 9,599 | |
| Cloth, sold at contract value ; unsold at market value ... | 18,50,936 | |
| | 32,39,319 | |
| Cloth with Selling Agents at selling prices | 365 | 32,39,684 |

**11. The Kohinoor Mills Co., Ltd. B/S. as on 31st December 1940**

| | Rs. | Rs. |
|---|---|---|
| **Stock-in-Trade** (as per Agents certified inventories | | |
| Cotton, Silk and other yarn— | | |
| Cotton at cost ... | 30,93,060 | |
| Silk and other yarn (purchased) at average cost ... | 5,62,197 | |
| Cloth, Yarn and Waste | | |
| Sold at contract price, unsold at or below market rates | 12,51,411 | 49,06,668 |

**12. Sitalpore Sugar Works, Ltd. B/S as on 30th June 1939**

| | Rs | Rs. |
|---|---|---|
| **Stock in Trade :—** | | |
| Stock of Sugar and Molasses— | | |
| Sugar ... | 3,54,028 | |
| Molasses ... | 2,353 | 3,56,381 |

*Note.*—No mode of valuation is given and the Auditor's Report is unqualified. The same mistake is repeated in the next balance sheet also.

**13. The Champarun Sugar Co., Ltd B/S. as on 30th June 1942**

| | Rs. | Rs. |
|---|---|---|
| **Stock-in-Trade :—** | | |
| Sugar (at Government control rates less Sugar Excise Duty) ... | ... | 6,25,211 |

**14. The Tata Chemicals, Ltd. B/S. as on 30th June 1944**

| | Rs. | Rs. |
|---|---|---|
| **Stock-in-Trade** (as per inventory certified and valued by the Managing Agents) | | |
| Salt and Chemicals-sold at contract rate | 22,797 | |
| Unsold at cost ... | 2,22,716 | 2,45,513 |

### 4. Book Debts.

This is a floating asset and stands for trading debts. Form F requires the following information to be given in the balance in respect of book debts :—

Book Debts :

(Distinguishing between those that are considered good and in respect of which the Company is fully secured and those considered good for which the company holds no security other than the debtor's personal security, and distinguishing between debts considered good and debts considered doubtful or bad. Debts due by directors and other officers of the company or any of them either severally or jointly with any other persons to be separately stated).

This detailed classification of the book debts of a company is intended to furnish the shareholders with information regarding the solvency or otherwise of its book debts. This is of particular importance in the case of banking companies, whose book debts consist of all loan debtors.

The law does not require that the trading debts of subsidiary companies should be shown separately.

How this asset is actually stated in the balance sheets will be clear from the following extracts :—

1. **The Tata Oil Mills Co., Ltd.—B/S. as on 31st March 1941.**

| **Book Debts :—** | Rs. | Rs. |
|---|---|---|
| Secured } (Considered good) | 2,28,445 | |
| Unsecured } | 2,99,631 | |
| Unsecured (Considered doubtful) | 994 | 5,29,070 |

2. **The Swan Mills, Ltd.—B/S. as on 31st December 1940**

| | Rs. |
|---|---|
| Book Debts (Unsecured-considered good) | 73,275 |

3. **The Betjan Tea Co., Ltd.—B/S. as on 31st December 1940**

| **Book Debts :—** | Rs. | Rs. |
|---|---|---|
| Unsecured, considered good | 2,145 | |
| Due by the Mg. Agents (Unsecured-Considered good) | 455 | 2,600 |

4 **The British India Corporation, Ltd.—B/S as on 31st December 1940**

| **Book Debts-Considered good** | | Rs. | Rs. |
|---|---|---|---|
| Secured | ... | 5,50077 | |
| Unsecured | ... | 26,87,644 | 32,37,721 |

5. The Burrakur Coal Co , Ltd.– B/S. as on 31st December 1940

| | |
|---|---|
| Book Deb s (Unsecured) Considered good | Rs. |
| (of which due by Directors solely aod jointly with others Rs. 2,793) | 11,78,000 |

6 The Titaghur Paper Mills Co , Ltd —B/S as on 31st March 1940

| | | |
|---|---|---|
| Book Debts (Coosidered good) | Rs | Rs. |
| Secured ... | 3,14,523 | |
| Uosecured ... | 25,08,864 | 28 23,387 |
| (Debts due from firms in which Directors of the Company are partners amount to Rs 3,175) | | |

7. The Ahmedabad Electric Co., Ltd, B/S. as on 30th September 1940

| | | |
|---|---|---|
| Book Debts—(Considered good) | Rs. | Rs. |
| Sundry Debtors (secured ... | 17,344 | |
| do (Partly secured to the extent of Rs. 6,374) .. | 15,262 | |
| do (Unsecured) | 2,22,153 | |
| Due by Directors and Officers severally or jointly with any other person for sopply of eoergy etc. (Unsecured) | 510 | |
| Due by Monicipality and other recoverable expenditure against contracts (Unsecured) ... | 72,030 | |
| Due by Cantonment Authorities Unsecured) ... ... | 2,814 | 3,30,113 |

8. The Indian Iron & Steel Co , Ltd B/S. as on 31st March 1940

| | | |
|---|---|---|
| Book Debts (Considered good) | Rs | Rs. |
| Secured ... | 46,796 | |
| Uosecured ... | 60,28,902 | |
| Subsidiary Company (Unsecured) | 47,352 | 61,23,050 |

9. The Bank of India, Ltd. B/S, as on 31st December 1943

| | | |
|---|---|---|
| | Rs | Rs. |
| Cash Credits aod Demaod Advaoces ... | | 6,90,73,387 |
| Loans ... ... ... | | 6,30 02,189 |
| Bills Discounted and Purchased ... | | 30,68,415 |
| | | 13 51,43,991 |
| Particulars required by Act VII of 1913:— | | |
| 1. Debts considered good in respect of which the Bank is fully secured ... | 12,00,03,545 | |
| This amount includes debts (fully secured) due by firms in which a Director of the Baok is a partner or guarantor or debts due by Directors jointly with others Rs. 63,267. | | |

| | |
|---|---|
| *The total of maximum balances under this heading during the year was Rs. 9,93,794. | |
| 2. Debts considered good secured by the personal liability of one or more parties in addition to the personal security of the debtors ... | 1,50,49,116 |
| This amount includes:— | |
| Bills Discounted Rs 23,17,250. | |
| Debts due by joint stock companies guaranteed by their agents, a director of the Bank being a member of the firm of Agents Rs. Nil. | |
| *The total of maximum balances under this heading during the year was Rs. 30,61,343. | |
| Debts due by Directors jointly with others Rs. Nil. | |
| *The total of maximum balances under this heading during the year was Rs Nil. | |
| 3. Debts considered good for which the Bank holds no security other than the debtors' personal security ... | 91,330 |
| 4. Debts considered doubtful ... | Nil |
| 5. Debts considered bad ... | Nil |
| | 13,51,43,991 |

*This information is required by form F, in connection with the asset 'advances' explained below.

## 5. Advances.

Form F requires that 'Advances' should appear in the balance sheet of a company as *follows* :—

Advances :

(Recoverable in cash or in kind or for value to be received, e.g. rates, taxes, insurance, etc., showing separately—

(a) loans given to subsidiary companies,

(b) loans including temporary advances made at any time during the year to directors or managers of the company).

This item of advances includes prepaid expenses, loans and deposits, which need not, however, be separately shown. Loans given to subsidiary companies and loans including temporary advances given to directors and managers of the company should be stated separately. The words 'loans including temporary advances made at any time during the year' are not free from ambiguity. On the one hand the term 'advances recoverable' means only the balances outstanding on the date of the balance sheet and not amounts already recovered; while on the other, it is thought that the intention of the law is to state in

tbe balance sheet hy way of a note the maximnm amcunt of advances outstanding at any time dnring the year along witb tbe actual balances ontstanding at the date of the balance sheet. It is, however, only a few banking companies wbich adopt the latter method.

Loans to Directors and managers may exist only in the case of private companies (which are not snhsidiary to a pnhlic company) and hanking companies. as nnder section 86-D loans to directors are probibited in other cases, while section 87 D does not apply to a private company (not being the suhsidiary of a pnhlic company) and does not prohibit any limited credit held by the managing agents in current account for the pnrpose of the company's bnsiness.

*In the case of companies other than banks, it is* not necessary to classify advances into secnred, nnsecnred, good, donbtful or bad; bnt in the case of a hanking company this will have to be done, becanse tbe advances are a part of its book dehts.

The following examples show clearly how advances are shown in the balance sheets :—

1. The Ahmedabad Electricity Co., Ltd. B/S. as on 30th September 1940

| | |
|---|---|
| Advances :— | Rs. |
| Insurance Premia, Telephone Rent, Deposits etc. | 30,498 |

2. *The Borrea Coal Co., Ltd. B/S.* as on *31st December 1940*

| | | | |
|---|---|---|---|
| Advanees :— | | Rs. | Rs. |
| Recoverable in Cash | ... | 8,888 | |
| For valne to be received | ... | 5,772 | 14,660 |

3 Smith, Stanistreet & Co., Ltd. B/S as on 30th June 1940

| | | | |
|---|---|---|---|
| Advances :— | | Rs. | Rs. |
| Recoverable in Cash-Deposits | ... | 14,574 | |
| For valne to be received | ... | 32,863 | 47,437 |

4. The Bombay Dyeing and Mfg. Co., Ltd. B/S as on 31st December 1940

| | | |
|---|---|---|
| Advances :— | Rs | Rs. |
| (i) Prepaid Expenses ... | 25,477 | |
| (ii) Loans given to Subsidiary Company | 1 10,000 | 1,35,477 |

5. The Bnrrakur Coal Co , Ltd. B/S as on 31st December 1940

| | | | | |
|---|---|---|---|---|
| Advances :— | | | Rs. | Rs |
| Recoverable in cash | ... | | 23,750 | |
| For value to be received | ... | | 19,517 | 43,267 |
| Loans secnred by Mortgage of Katras Property | ... | | 10,56,578 | |
| Other Loans :— | | | | |
| Secured | ... | 4 57,553 | | |
| Unsecnred | ... | 22,758 | 4.80,311 | 15,36,889 |

6. The Associated Cement Co., Ltd. B/S as on 31st July 1940

| Advances :— | Rs. | Rs. |
|---|---|---|
| Sundries, including Deposits and Advances against tenders, contracts, etc. | 3,94,734 | |
| Option moneys paid for purchase of land ... | 4,880 | |
| *Prepaid Expenses* ... | 43,080 | 4,42,694 |

7. The Kumardhubi Fireclay and Silica Works Ltd.
B/S. as on 31st December 1939

| Advances :— | Rs. | Rs. |
|---|---|---|
| For value to be received | 1,025 | |
| To be recovered in cash ... | 7,318 | 8,343 |
| (Advances considered doubtful Rs 1,575) | | |
| Deposits ... | | 2,224 |

8. The Tata Oil Mills Co., Ltd. B/S. as on 31st March 1945

| Advances:— | Rs. | Rs. |
|---|---|---|
| Prepaid Expenses .. | 80 836 | |
| To contractors and others ... | 6,57,571 | |
| Against purchase of Raw Materials, Machinery, etc. ... | 72,096 | |
| Payment *of* I. T. & C. T. *for* 1944–45 under Section 18 A of the Indian Income-Tax Act ... | 5,67,978 | 13,78,481 |

## 6. Investments.

Form F requires the following information to be given in the balance sheet of a company with regard to investments :—

Investments :—

(Showing nature of investments and mode of valuation, e. g., cost or market value and distinguishing :—

*(a)* investments in government or trust securities,

*(b)* investments in shares, debentures or bond showing separately shares fully paid up and partly paid up,

*(c)* investments in shares, debentures or bonds of subsidiary companies,

*(d)* immovable properties.

Not only banks but also all good industrial companies carry a large *portfolio* of investments in India. The law requires that the nature of investments and the mode of their valuation must be detailed in the balance sheet. The investments are to be classified under the four heads given above, though it is not necessary to describe each investment *separately*. *In* practice some companies detail the nature of each security, while others follow the letter of the law and put only the total under each head.

The mode of valuation of investment given in the balance sheet is useless unless sufficient information is supplied, e. g., if the investments are valued at cost, an indication of their market value on the date of the balance sheet should also be given

The interest accrued on investments is a separate item in Form F; but it may be added to investments if so desired.

The following are the examples showing how this asset figures in the balance sheets of Indian companies :—

**1. The Clive Buildings (Calcutta), Ltd. B/S. as on 31st December 1940**

| | | | Rs. | Rs. |
|---|---|---|---|---|
| **Investments at Cost :—** | | | | |
| Rs. 50,000 4% Govt. Loan | | 1943 | 50,875 | |
| Rs. 25,000 $3\frac{1}{2}$% | do | 1947–50 | 26,641 | |
| Rs. 40,000 3% | do | 1941 | 41,531 | |
| Rs 25,000 $2\frac{3}{4}$% | do | 1948–52 | 24,312 | 1,43,359 |

(Market value on 31–12–1940 Rs. 1,42,266)

**2. The Bombay-Burmah Trading Corporation, Ltd.**
**B/S. as on 31st May 1940**

| | Rs. | Rs. |
|---|---|---|
| **Investments :—** | | |
| Indian and Sterling Securities at market price ... | 29,46,580 | |
| Shares in Companies fully paid at cost | 1,76,832 | |
| *Shares in Subsidiary Companies at cost | 26,74,000 | |
| | 57,97,412 | |
| *Less* Investment Reserve | 5,82,030 | 52,15,382 |

* This Company has two subsidiary companies and the holding in each is not separately stated.

**3. The Burrakur Coal Co., Ltd. B/S. as on 31st December 1940**

| | | Rs. | |
|---|---|---|---|
| **Investments at or under cost :—** | | | |
| Invetments in Government Securities :— | | | |
| Rs. 3,55,000 3% Defence Bonds 1946 ... | 3,55 000 | | |
| Rs. 60,400 $3\frac{1}{2}$ % Loan 1947–50 | 59,834 | | |
| Rs. 25,000 5°/ₒ Loan 1945–55 | 25,000 | | |
| Rs. 11,000 5°/ₒ U. P. Bonds 1944 | 11,000 | 4,50,834 | |
| Invesments in shares :— | | | |
| 1,200 Ordinary Shares in the Deshergarh Power Supply Co, Ltd at Rs. 100 each | 1,20,000 | | |
| 50 Shares in the Reserve Bank of India at Rs. 100 each | 5,000 | 1,25,000 | |

| | | Rs. | Rs. |
|---|---|---|---|
| Investment in Shares of Subsidiary Companies:— | | | |
| 1,19,997 Ordinary Shares in the Sijua (Jherriah) Electric Supply Co., Ltd. of Rs. 10 each of which Rs. 5 is paid up ... | 5,99,985 | | |
| 25,000 Ordinary Shares in the Kumardhubi Fireclay and Silica Works, Ltd., at Rs 10 each ... | 2,50,000 | 8,49,985 | |
| Government Securities deposited against contracts :— | | | |
| Rs. 30,000 $3\frac{1}{2}$% Loan 1947–50 (Market value Rs. 15,62,250) | | 29 719 | 14,55,538 |

4. **The British India Corporation, Ltd. B/S. as on 31st December 1940**

| | | Rs. | Rs. |
|---|---|---|---|
| **Investments at or under market value :—** | | | |
| Government Loans | ... | 3,08,694 | |
| Commercial Debentures | ... | 5,51,300 | |
| Commercial Preference Shares | .. | 5,82,837 | |
| *Commercial Ordinary Shares* | ... | 7,08,548 | |
| Shares in Subsidiary Company | ... | 1,63,958 | 23,15,337 |

5. **The Clive Mills Co., Ltd. B/S. as on 31st March 1940**

| | Rs. | Rs |
|---|---|---|
| **Investments at or under market value :—** | | |
| Rs. 1,00,000 $3\frac{1}{2}$% Loan 1947–50 (of the above Securities for Rs. 92,000 deposited with the Indian Jute Mills Association) | 92,500 | |
| 250 Ordinary Shares in the Sonakunda Baling Co., Ltd. | 25,000 | |
| 50 Shares in the Reserve Bank of India ... | 4,850 | 1 22,350 |

6. **The Ryam Sugar Co., Ltd B/S. as on 30th June 1940**

| | Rs. | Rs. | Rs. |
|---|---|---|---|
| **Investments—(at or under cost)** | | | |
| **General—** | | | |
| Govt. Securities (Deposited as security) ... | 4,951 | | |
| Shares and Debentures fully paid ... | 10,600 | 15,551 | |
| **Debenture Sinking Fund—** | | | |
| Govt. Securities ... | 24,936 | | |
| Debentures fully paid ... | 1,59,930 | 1,84,866 | 2,00,417 |

**7. The Pankaja Mills, Ltd. B/S. as on 31st December 1943**

| Investments :— | Rs. | Rs. |
|---|---|---|
| Excess Profits Tax Refund Deposit | 2,06,985 | |
| 50 Shares in Madras Handloom Weavers' Provincial Cooperative Society, Ltd. at cost ... | 2,500 | |
| Government of India 3% Defence Bonds at cost ... | 1,00,792 | 3,10,277 |

*Notes.* 1.—The E. P. T. Deposit under Section 10 of the Indian Finance Act of 1942 is usually shown as a separate asset after the Investments, although in this case it is put under Investments.

2.—In the case of shares it is not stated whether they are fully paid or partly paid, although it is so required by law.

### 7. Cash and Other Balances.

From F requires this asset to be shown in the balance sheet as under :—

Cash and Other Balances :—

Amount in hand

Balances with agents and bankers (In detail showing whether on deposit or current account, etc.)

Note that it is 'Cash and Other Balances' and not merely 'Cash and Bank Balances'. So it includes cash in hand and balances with agents and banks The names of banks in which the balances are held need not be stated, but the nature of balances must be detailed.

The following extracts from actual published accounts will show how this item appears in the balance sheets :—

**1. The Tata Oil Mills, Co., Ltd. B/S. as on 31st March 1941**

| Cash and other Balances :— | Rs. | Rs. |
|---|---|---|
| In hand at Head Office, Factories and Depots ... | 13,751 | |
| In Transit ... | 16,462 | |
| With Banks on Current Accounts | 97,091* | |
| Deposits with Railways, Hospitals, Post-Trust, Municipalities etc. | 28,563 | 1,55,867 |

*This includes a sum of Rs 4,918 with the Travancore National and Quilon Bank, Ltd. (in Liquidation)

**2. The Ryam Sugar Co., Ltd B/S. as on 30th June 1940**

| Cash and other Balances :— | | Rs | Rs. |
|---|---|---|---|
| With Imperial Bank of India | | | |
| On Staff Security Deposit | 6,700 | | |
| On Current Account | 3,009 | 9,709 | |
| With Mg. Agents on Current Account | | 15,928 | |
| In Transit ... | | 12,000 | |
| In hand at Factory ... | | 10,195 | 47,832 |

3. The Finlay Mills, Ltd. B/S. as on 31st December 1940

| Cash and other Balances :— | | Rs. | Rs. |
|---|---|---|---|
| In hand | ... | 7,303 | |
| At the Mill | ... | 737 | |
| With the Bank of India, Ltd. on Current Account | ... | 206 | |
| With The Imperial Bank of India Savings Bank Account (on account of Staff Security Deposit. | ... | 3,443 | |
| With the National Bank of India, Ltd. against letter of guarantee | ... | 150 | |
| Deposit with the East India Cotton Association, Ltd. | ... | 5,000 | 16,839 |

4. The Tata Chemicals, Ltd.—B/S. as on 30th June 1944.

| Cash and other Balances :— | | Rs. | Rs. |
|---|---|---|---|
| In hand ... | ... | 5,881 | |
| In Current Account with Banks | ... | 2,88,351 | |
| On Deposit with Bank against letters of credit covering American orders | ... | 78,662 | |
| In Current Account with foreign agents for purchase of machinery | ... | 6,373 | 3,79,267 |

5. The Beljan Tea Co., Ltd.—B/S. as on 31st December 1940.

| Cash and other Balances :— | | Rs. | Rs |
|---|---|---|---|
| With the Allahabad Bank. Ltd on Deposit | | 75,000 | |
| With the Hongkong and Shanghai Banking Corporation on Deposit | ... | 25,000 | |
| With the Chartered Bank of India Australia and China on Deposit | ... | 25,000 | |
| With the Imperial Bank of India on Dividend Accounts | ... | 1,663 | |
| With the Managing Agents on Current Account | ... | 7,414 | |
| With the Imperial Bank of India on Current Account ... | ... | 99 | |
| With Garden Manager | ... | 177 | 1,34,353 |

6. The British India Corporation. B/S. as on 31st December 1940.

| Cash and other Balances :— | | | |
|---|---|---|---|
| In hand .. | ... | 2,83 267 | |
| On Current Account with Banks | ... | 22,59,078 | |
| On Security Deposit Account with Bank | | 3,238 | |
| With London Office ... | ... | 13,534 | 25,59,117 |

**7. The Titaghur Paper Mills Co., Ltd. B/S. as on 31st March 1941.**

| | Rs. | Rs. |
|---|---|---|
| Cash and other Balances :— | | |
| Deposited with Chartered Bank of India, Australia and China ... ... | 7,50,000 | |
| Deposited with Chartered Bank of India, Australia and China ... ... | 32 050 | |
| (Account Staff Security in accordance with Section 282 B (1) of Indian Companies Act) | | |
| Chartered Bank of India, Anstralia and China on Current Account ... | 60,683 | |
| Imperial Bank of India on Current Acconnt | 4,936 | |
| Allahabad Bank on Current Account .. | 129 | |
| Central Bank of India on Current Account | 13,212 | |
| Cash on Current Account with Managing Agents ... ... | 15,344 | |
| Cash at Bamboo Forest Offices ... | 9,255 | |
| Cash at Mills Offices ... ... | 322 | 8,85,931 |

**8. The Bengal Paper Mill Co , Ltd. B/S. as on 31st December 1940.**

| | | |
|---|---|---|
| Cash and other Balances :— | | |
| With Banks | | |
| On Deposit ... ... | 2,00,000 | |
| On Current Account ... ... | 1,13,668 | |
| On Employees, Security Deposit Account ... ... | 19,343 | |
| With Mill Manager ... ... | 660 | |
| With Managing Agents ... | 1,582 | 3,35,253 |

### 8. Information regarding Subsidiary Companies

A recent development in industry and commerce has been the advent of the holding company. A holding company is one that acquires a controlling interest in the affairs of the other companies, which companies are known as the subsidiary companies. The object of acquiring such control is usually to weld all the companies into one combine, to the mutual advantage of all, but particularly of the holding company.

**Legal Definition**—Section 2 (2) provides that where a company *holds* shares in another company directly or through a nominee *and*

(*a*) The amount of shares held is more than 50 per cent. of the issued share capital of the other company except where the shares are held as security by a company the ordinary business of which is the lending of money, *or*

(*b*) The share holding is such as to entitle the company to more than 50 per cent of the voting power in the other company, *or*

(*c*) The company has power directly or indirectly to appoint the majority of the directors of that other company otherwise than by virtue of the provisions of a debenture trust deed,

this latter company is called a subsidiary company, and subsidiary company includes a *subsidiary company of its own.* The words "and includes a subsidiary company of its own" are very important, since they expressly provide that a subsidiary company will include its own subsidiaries. In the absence of these words it would appear that where the A Company holds a controlling interest in the B Company and the B Company holds a controlling interest in the C Company, the C Company is not a subsidiary of A Company (even though the A Company *indirectly* has the power to appoint the majority of the directors of the C Company unless the A Company holds some shares in the C Company.

There is, however, no legal definition of a holding company. But the definition of a holding company directly follows from that of a subsidiary company as given above. A holding company is, therefore, one which has an interest (as defined above) in one or more subsidiary companies. Although any company which holds shares in another company may be called a holding company, yet the term holding company is legally confined to companies which hold shares in subsidiary companies within the meaning of this section.

It is possible that a subsidiary company may at one time be the subsidiary of more than one holding company. Thus, if a company has a share capital consisting of 1,200 preference shares of Rs. 100 each (carrying one vote per share) 10,000 ordinary shares of Rs. 10 each (carrying one vote per share), and 8,000 deferred shares of Re. 1 each (carrying one vote per share and the right to appoint 60 per cent. of the directors) and each class of shares is held by a different company, then the A Company is a subsidiary company of three holding companies, because one holding company holds more than 50 per cent. of the issued share capital, the second holds more than 50 per cent. of the voting power, and the third holds the right to appoint the majority of the directors.

**Information regarding Subsidiary Companies.** Under section 132 (2), the balance sheet of a holding company (which must be in conformity with the provisions of Form F) must disclose separately (i) the secured loans due to subsidiary companies, (ii) the unsecured loans due to subsidiary companies, and (iii) the investments in the shares, debentures and bonds of subsidiary companies In each case only the aggregate amount is to be stated. It is not necessary that the figures relating to each subsidiary company should be separately given. With regard to investments in subsidiary companies, it would however, be better from the point of view of the shareholders of the holding company, if the details of investment in each subsidiary company were set out separately. Further, the trading debts due by or to subsidiary companies are not to be shown separately in the balance sheet of the holding company.

Section 132—A requires the following further information regarding the affairs of subsidiary companies to be disclosed in the published accounts of a holding company other than an investment company :—

*(a)* The last audited balance sheet and profit and loss account together with the auditor's report of each subsidiary company are to be attached to the balance sheet of the holding company. It means that the share holders of the holding company are to be supplied with

the annual accounts of each subsidiary company along with the annual accounts of the holding company. This is the only method by which the shareholders of the holding company may be kept informed about the affairs and the financial position of each subsidiary company.

*(b)* There should be annexed to the balance sheet of the holding company a statement signed by the same persons as are required by section 133 to sign the balance sheet of the holding company and showing:—

(i) How the profits and losses of a subsidiary company or the aggregate profits and losses where there are two or more subsidiary companies have been dealt with in or for the purpose of the accounts of the holding company; and

(ii) To what extent provision has been made for the losses of any subsidiary company, either in the accounts of that company or of the holding company or of both, and to what extent the losses of any subsidiary company have been taken into account by the directors of the holding company in arriving at the profits and losses of the holding company as disclosed in its accounts; and

(iii) The qualifications, if any, that may be found in the auditor's report of any subsidiary company.

It is not necessary to specify in any such statement the actual amount of the profits or losses of any single subsidiary company, or the amount of any part thereof that has been dealt with in any particular manner, nor does the section define the manner in which the profits and losses of subsidiary companies are to be treated by the holding company. In any event, the statement to be annexed to the balance sheet of the holding company must disclose the method that has been adopted by the holding company in regard to the profits and losses of its subsidiary companies.

If for any reasons the directors of the holding company are unable to obtain such information as is necessary for the preparation of the statement, the directors who sign the balance sheet must so report in writing and their report should be annexed to the balance sheet in lieu of the statement.

There is a contradiction in this section, for while it provides that the statement need not disclose the actual amount of the profits or losses of any subsidiary company, yet the last audited balance sheet and profit and loss account with the auditor's report of each subsidiary company are to be annexed to the balance sheet of the holding company. Moreover, the inclusion in the statement of the qualifications found in the auditors' reports of subsidiary companies is quite unnecessary in view of the fact that the auditors' reports themselves are to be circulated to the members of the holding company.

In this connection, it may also be pointed out that the exemption of investment companies from the provisions of section 132-A is open to criticism, because in the event of an investment company taking up so large an interest in one direction as to become a holding company, the necessity for acquainting its shareholders with details

of the position would be no less than in the case of a trading company. One can also imagine that it might be possible to avoid the plain intention of the law by so framing a memorandum of association as to make a trading company in form, though not in fact, an investment company.

The statement regarding subsidiary companies, above referred to, usually appears either as a footnote on the balance sheet of the holding company or as a note under the 'Investment in Subsidiary Companies'. It is, however, sometimes included in the directors' report instead of in the balance sheet of the holding company; and there can be no objection to this practice so long as the directors' report is signed by the same persons as are required to sign the balance sheet, because the directors' report itself is, under section 131-A, a part of the balance sheet. The following are the examples of this statement taken from the published accounts of Indian companies :—

1. **The National Insurance Co, Ltd.** Directors' Report for the year ended 31st December 1942.

   "Statement pursuant to Section 132-A. The National Fire and General Insurance Co., Ltd., has not declared any dividend during the period under report and the credit balance of the Profit & Loss Appropriation Account has been carried forward in the Accounts of that Company."

2. **Onurepore Co., Ltd.** Directors' Report for the half-year ended 31st March 1942.

   "The dividend in respect of the holding in the subsidiary company which has been credited to Profit & Loss Account is that which it is proposed be declared out of the profits for the half-year to 31st March 1942."

3. **The Burrakur Coal Co., Ltd.** Directors' Report for the half-year ended 31st December 1940.

   "Subsidiary Companies—Pursuant to Section 132-A of the Indian Companies Act, the Balance Sheets as at 31st December 1939 and relative Profit & Loss Accounts of the Sijna (Jherrian) Electric Supply Co, Ltd. and the Kumardhubi Fireclay & Silica Works, Ltd., are appended. The profits of the subsidiary companies were credited to the Profit & Loss Account of the Burrakur Coal Co., Ltd., to the extent of dividends received, in the accounts for the half-year ended 30th June 1940."

4. **The Titaghur Paper Mills Co., Ltd.** Directors' Report for the half-year ended 30th September 1942.

   "Pursuant to Section 132-A of the Indian Companies Act, the Balance Sheet as at 30th September 1942 and relative Profit & Loss Account of Messrs. Commercial Products, Ltd, are appended. The credit balance on that account has been carried forward."

5. **The Bombay Dyeing & Mfg. Co, Ltd.** Balance Sheet as on 31st December 1940 under the item 'Investments'.

   "No provision has been made in the accounts of the Company for the debit balance carried forward in the Profit & Loss Account by The Nowrosji Wadia Ginning and Pressing Co, Ltd."

6. **The Indian Iron & Steel Co., Ltd.** Balance Sheet as on 31st March 1940.

"Nothing is included by the Company in respect of the profits made by the subsidiary companies for the year to 31st March 1940 In the one case the profit has been utilised in reducing the debit balance on Profit & Loss Account, while in the other the balance has been carried forward in the books of the subsidiary company.

"In one company the Auditors' Report has been qualified as follows :—'Subject to the observation that no provision has been made for Depreciation'."

7. **The Associated Cement Companies, Ltd.** Balance Sheet as on 31st July 1940.

"No portion of the profits of the Patiala Cement Co , Ltd., and The Cement Marketing Co. of India, Ltd., (Subsidiaries of this Company) for the period ended 31st March 1940 have been taken credit for in the Profit & Loss Account."

8. ***The Central Bank of India, Ltd.*** Directors' Report for the year ended 31st December 1944.

"Statement pursuant to Section 132-A of the Indian Companies Act· The profits of two of the Subsidiary Companies of the Bank, namely, The Central Bank Executor and Trustee Co., Ltd., and The Depositors' Benefit Insurance Co., Ltd., respectively for the year ended 31st December 1943, have been included in the item 'By Interest, etc.' in the Profit & Loss Account to the extent of the dividends (in respect of the Bank's shareholdings) declared and paid by the said Subsidiary Companies. Undistributed balances of the two above-named Subsidiary Companies have been carried forward or otherwise dealt with in the accounts of such Companies"

### 9. The Auditor's Report.

Under section 131 (2) the balance sheet and the profits and loss account of a company must be audited by the auditor of the company, and the auditor's report must either be attached to the balance sheet and the profit and loss account or it may be given as a separate document, but in the latter case a reference to it must be inserted at the foot of the balance sheet and the profit and loss account. In practice, however, the auditor's report is, save in very exceptional cases, invariably attached to the balance sheet of the company ; because, when a copy of the auditor's report is to be circulated to the members under the provisions of section 131 (3), there is no point in keeping it separate from the balance sheet.

Shareholders and other interested parties have thus been given the legal protection of the auditor's report on the balance sheet and profit and loss account of a company. Section 144 provides for the appointment of auditors at each annual general meeting to hold office until the next annual general meeting. Special provisions are made by law to ensure that there shall always be an auditor The directors can appoint an auditor only before the statutory meeting (to act until the first annual meeting) or to fill a subsequent casual vacancy until the next general

meeting. They cannot, however, depose an auditor. At every annual general meeting (and if there are half yearly meetings; at the first half-yearly meeting held in the year) an auditor or auditors must be appointed; and if the appointment is not made, the Provincial Government will make it on the application of any member of the company. Only the retiring auditor can be appointed at an annual general meeting unless notice of the nomination of a new auditor has been given to the members and the retiring auditor not less than seven days before the meeting. The member who desires to nominate a new auditor must give notice of his intention to the company not less than fourteen days before the meeting.

**Auditor's Duties.** Under section 145 (2) the auditor of a company is required to make a report to the members of the company on the accounts examined by him and on every balance sheet and profit and loss account laid before the company in general meeting during his tenure of office. The chief value of the auditor's report lies in its check on the accuracy of the figures presented. It does not in itself add anything to the information disclosed.

Generally speaking, the duty of the auditor is to make what he considers a *sufficient* examination of the books and other records that lead up to the balance sheet and the profit and loss account to be laid before the shareholders in general meeting, and, on the basis of this examination and any explanations he thinks it necessary to require, to report to the shareholders. He is the agent of the shareholders and is appointed for their benefit and not for the benefit of the directors.

He is not expected to guarantee the accuracy of every detail of the company's books, nor is he supposed to act on the assumption that fraud or serious error exists in the accounts and carry out an investigation with a view to running it to earth and discovering the culprits. He is a watchdog, but not a bloodhound. All that he is employed to do is to say whether or not he thinks that the company's financial position is truly exhibited to the shareholders.

The duties of an auditor, as laid down by law, are not subject to anything the members of the company may agree or that the articles of association may prescribe. They are a minimum; and although they may be added to by the articles, they cannot be reduced. Members cannot, therefore, cast away the protection that is given them by law.

***The Auditor's Report.*** The report which an auditor is required to make under section 145 (2) must state—

(*a*) Whether or not he has obtained all the information and explanations he has required, and

(*b*) Whether or not in his opinion the balance and the profit and loss referred to in the report are drawn up in conformity with the law; and

(*c*) Whether or not such balance sheet exhibits a true and correct view of the state of the company's affairs according to the best of his information and the explanations given to him, and as shown by the books of the company; and

(*d*) Whether in his opinion books of account have been kept by the company as required by section 130.

Where any of the matters referred to above is answered in the negative or with a qualification, the report must state the reason for such answer.

The same section provides that the auditor shall have a right of access at all times to the books and accounts and vouchers of the company and shall be entitled to require from the directors and officers of the company such information and explanations as may be necessary for the performance of his duty as auditor.

The following are the circumstances in which an auditor may find it necessary to qualify his audit report to the members :—

(*a*) Where access to any books or accounts or vouchers of the company has been refused to him, or where he has not been able to obtain any information or explanations that he may have required from the directors and officers of the company.

(*b*) Where the balance sheet and the profit and loss account on which he has reported are not in his opinion drawn up in conformity with the law.

(*c*) Where the balance sheet does not exhibit a true and correct view of the state of the company's affairs, as, for example, where he has been unable to verify any asset or liability of the company, where any assets are improperly valued, where the provision for depreciation is inadequate, where any known losses or liabilities are not sufficiently provided for, or where any excessive and unjustified secret reserves exist

(*d*) Where proper books of account as required by law have not been kept by the company.

In the case of Indian companies owning factories, mines and works, situated at a considerable distance from the registered office of the company or from the central management, it is a common practice with the auditors to examine the books kept at the registered office or at the office of the central management, whilst the returns submitted by branches, works, factories, etc., are accepted on the signature of the local manager, and this fact is referred to in the auditor's report.

If an auditor finds it necessary to insert any qualification in his *audit report, he must state the reason for it. Further*, the *auditor*, when giving a qualified report, should be guided by the dictum of Lindley. L. J. *in Re The London and General Bank*, who said : "A person whose duty it is to convey information to others does not discharge that duty by simply giving them so much information as is calculated to induce them to ask for more. Information and the means of information are by no means equivalent terms."

Below are given some qualified auditors' reports which have appeared on the published accounts of Indian companies.

1. "We report that we have audited.........with the Books and Accounts as kept in Calcutta and at the Works in which are incorporated the certified returns from the mines and the London Transfer Office, and have obtained........" The Indian Iron and Steel Co., Ltd. —Accounts for the year ended 31st March 1940.

2. "........and such Balance Sheet, subject to the provision of adequate depreciation on fixed capital expenditure, exhibits..........." The New Victories Mills, Ltd —Accounts for the year ended 31st December 1940

3 'Subject to the observation that the market value of the investments is greatly in excess of the value shown, the Balance Sheet exhibits........" The Muir Mills, Co Ltd.,—Accounts for the year ended 31st December 1940.

4 "Following previous practice, the stock of stores on hand at the Delhi Cloth Mills on 30th June 1940 has continued to be valued at 50°/₀ of cost, although consequent upon the outbreak of war considerable purchases were made during the latter part of the year.

"Subject to the foregoing remarks and to the provision of adequate depreciation, such Balance Sheet exhibits ........" The Delhi Cloth and General Mills Co., Ltd.—Accounts for the year ended 30th June 1940.

5 'We have accepted the allocations to Capital Expenditure and Revenue Expenses in respect of labour employed and stores issued on various works as passed by the Engineer-in-Charge at Ajmer and countersigned by the Managing Director.

"Subject to an adequate provision for depreciation of fixed assets from March 1931 to date, such Balance Sheet exhibits........" The Ajmer Electric Supply Co., Ltd.—Accounts for the year ended 31st March 1941.

It must be remembered that the duties imposed upon a company auditor by law may be extended by the articles. In such a case the auditor must comply with the provisions of the law as well as the articles. The following is an example of an auditor's report in which certain matters required by the company's articles are included in addition to those required by law :—

"We have audited the foregoing Balance Sheet of The Bombay-Burmah Trading Corporation, Limited, as at the 31st May 1940 and also the foregoing Profit & Loss Account for the year ended on that date, in which are incorporated the audited returns from Rangoon, Moulmein, Bangkok, Mudis and Munjolai and beg to report that --

(a) We have obtained all the information and explanations we have required, including such as have been called for from Directors or other officers of Corporation, which have been given and which have been satisfactory ; and

(b) In our opinion the foregoing Balance Sheet and Profit & Loss Account are drawn up in conformity with the law ; and

(c) Such Balance Sheet is in our opinion full and fair, containing the particulars required by the Articles of Association, and exhibits a true and correct view of the state of the Corporation's affairs according to the best of our information and the explanations given to us and as shown by the books and afore mentioned returns of the Corporation ; and

(d) In our opinion books of account have been kept by the Corporation for the period under report as required by Section 130 of the Indian Companies Act."

## CHAPTER 4.

### THE PROFIT AND LOSS ACCOUNT

In the case of businesses owned by individuals and partnerships, the proprietors may ascertain their profits in any way they like, because other parties are not interested therein; but with regard to companies the case is different. Besides the present shareholders of a company there are other persons, such as the prospective shareholders, debenture-holders and creditors, employees, etc, who are interested in its profits Therefore it is very important that the profits of a company are properly computed; otherwise the varions parties would be affected as follows :-

1. If the profits are overstated and if the whole amount thereof is distributed as dividend, the dividend will be paid ont of capital to the extent of the amount by which the profits are overstated; and in that case the directors of the company will be personally liable to acconnt for any dividends so paid ont of capital Moreover, when any dividend is paid out of capital, it amounts to a reduction of capital in contravention of section 55 of the Indian Companies, Act, for which every director and other officer of the company is liable to a fine up to Rs. 1,000.

2. Any dividend improperly paid owing to an excessive statement of profits will adversely affect the interests of debenture-holders and creditors by depleting the assets of the company to which they look for the payment of their claims.

3. If the profits are nnderstated they will have the effect of depriving the present shareholders of dividends to which they are entitled and of depressing the market value of their shares.

4 Sometimes third parties such as directors, managers and managing agents, receive a part of their remuneration by way of a percentage based on the profits of the company. If the profits are under stated, the remuneration payable to such persons will be less than what it should be; where an overstatement of profits will result in an excessive remuneration being paid to them, thereby causing a corresponding loss to the company.

5 If, through an overstatement of profits, dividends are paid out of capital, the capital of the company will in course of time be drained, and the company will become insolvent and may have ultimately to go into liquidation.

The profit and loss account is the acconnt by which the directors disclose to the shareholders the result of the actual working of the company. It serves to give to the shareholders an idea of the earning capacity of the company in relation to its capital and is an important factor in enabling them to judge about the administration and management of the affairs of the company by the directors

Generally speaking, the information given in the profit and loss account, however abbreviated in form, is of as much value to the shareholders in affording a guide to the company's position and progress as the information contained in the balance sheet, however much greater in volume the latter information may be. After all, the value of the assets of a business considering as a whole, really depends on what they are capable of earning in the form of annual profit; and consequently the figure of net profit which should be shown in a profit and loss account, when considered in conjunction with similar figures relating to previous financial years, may give the shareholders a fairly true indication of the real value of the enterprise which the company owns.

**Compulsory Profit & Loss Account.** The Indian company law is in advance of the English company legislation as far as the publication of a profit and loss account is concerned. Since 15th January 1937, when the Indian Companies (Amendment) Act of 1936 came into force, it has been compulsory for every public company to publish a profit and loss account containing the prescribed information. When this amending bill was on the legislative anvil in 1936, there was a very heated debate in the Central Legislative Assembly on the issue of a compulsory profit and loss account, and the following arguments were put forward for and against the proposal :–

**Arguments for compulsory Profit & Loss Account.**

1. A profit and loss account must contain such particulars as will give a person looking at it a good idea as to how the profit or loss has been arrived at. The details of the working and administration of a company must be disclosed to the shareholders

2. Regulation 107 of Table A which lays down the contents of a profit and loss account, is very modest in its terms. As to the way in which the details of the profit and loss account may be assessed or assorted discretion is entirely left in the hands of the directors.

3. Profit and loss accounts of various companies have been published in the past without legal compulsion; and details have been given of the working of companies without any harm.

4. In the absence of statutory requirements, it will be easy to cover up a profit and loss account and not to show a true profit and loss account to the shareholders. For example, a large amount may be spent by way of establishment, much more than ordinarily ought to be paid for service, and thus there would not be any opportunity for the shareholders to regulate the amount of expenditure with respect of which they have got a right to impose conditions on the directorate.

5. When the term office of the managing agents has been restricted to twenty years, it is possible (in the absence of any statutory requirements) that they may resort to a lot of window-dressing and make appear that all is well until the crash comes ultimately. Therefore it is desirable that sufficient material should be placed in the hands of shareholders who are primarily interested in the affairs of the company to watch and give directions to the management.

6. It is desirable that in a country which has embarked upon discriminating protection the public should know as much as possible about the profits of the business or companies that are so protected.

7. It is not only shareholders who are interested in getting information regarding the working of a company, but there are other parties also who are interested. In the first place there are the employees of the company who are interested in knowing the details of the accounts of that company. Many times questions regarding wages of the employees arise and there are disputes. The employers generally plead that they have to spend money on other items, for instance, the prices for raw material have gone up or something else has happened and therefore the wages could not be increased. If an employer takes that attitude in a wage dispute it is necessary for the employees to know the details of the costs or other matters.

Then there is the general public interested in the accounts of a company, which comes to the legislature for concessions.

8. The utility of the profit and loss accounts depends on statutory insistence on the company's disclosing certain points and certain matters which ought to be disclosed in order to give the shareholders and the public a correct idea as to the state of the company's affairs and as to the way it has worked during the year.

### Arguments against compulsory Profit and Loss Account,

1. It is one thing to make a profit and loss account compulsory and quite another to stipulate for the disclosure of detailed figures. The statutory information to be provided in the profit and loss account will, in a large number of cases, be deterimental to the Interests of the company and consequently to the shareholders.

2. There are already a large number of provisions in the Act for the publicity and diclosure of information, and their cumulative effect is to give the shareholders a much better opportunity of knowing about the working of their company.

3. One of the arguments for the publication of a detailed profit and loss account is that a large number of companies already publish it, although they are not legally obliged to do so. That is certainly the case, but it follows that those companies which do so are naturally careful not to disclose information which would be of value to their competitors and deteiimental to themselves.

4. Another argument is that many companies already disclose full details of costs in their published figures. That is perfectly true, and it is, for example, a common practice among tea and rubber companies But in such cases it is evident that the company has nothing to fear from such diclosure and the information given cannot be made use of by others in the same line of business in a competitive. spirit.

5. It entirely depends on the nature of the business whether disclosure of costs can be safely made. In the coal industry, for example, where the disposal of a colliery's output may very often depend on an anna or two in the price per ton quoted, which in turn depends fundamentally on the raising costs, information about the costs of a competitor mining the same class of coal would be of the greatest value and might very well result in one colliery putting a a neighbour out of business or making things so difficult for him that there would be no profits to divide among the shareholders.

6. A compulsory profit and loss account had been introduced in England in 1929, but there was no form prescribed nor any rigid limit imposed as to the items which should be contained in the profit and loss account. It is left to the company to decide what details are to be given in the profit and loss account.

### Statutory Contents of Profit & Loss Account.

Section 17 (2) together with Regulation 107 of Table A and section 132 (3) deal with the contents of the published profit and loss account of a company. The form of the profit and loss account is not prescribed by law ; but certain essential information to be given therein is laid down. This may be considered under two headings.

1. Under *section 17 (2), Regulation 107 of Table A is* made compulsory for all companies including private companies. This regulation reads as follows :—

"The profit and loss account shall, in addition to the matters referred to in sub-section (3) of section 132 of the Indian Companies Act, 1913, show, arranged under the most convenient heads, the amount of gross Income, distinguishing the several sources from which it has been derived, and the amount of gross expenditure, distinguishing the expenses of the establishment, salaries and other like matters. Every item of expenditure fairly chargeable against the year's income shall be brought into account, so that a just balance of profit and loss may be laid before the meeting, and, in cases where any item of expenditure which may in fairness be distributed over several years has been incurred in any one year, the whole amount of such item shall be stated, with the addition of the reasons why only a portion of such expenditure is charged against the income of the year."

According to the second proviso to sub-section (2) of section 17, the concluding words "and, in cases .. . .......of the year" of Regulation 107 will not apply to a company which so determines in general meeting.

This regulation except for the recent addition of the words "in addition . .... . ...Indian Companies Act, 1913" has been included in Table A, or Table B as it then was, since 1857 and consequently it is difficult to determine the meaning intended by the legislature, and it is manifest that significance of certain words has altered during the period that has elapsed. The requirements of this regulation may now be analysed as follows :—

*(a)* The profit and loss account shall show, arranged under the most convenient heads, the amount of gross income, distinguishing the several sources from which it has been derived.

The term used is gross income and not gross profit. The former term is wider than the latter. Gross income is the income from the sale of goods and services and from other sources such as interest, rent, commission etc. The several sources from which the gross income has been derived are to be shown separately under convenient heads. If a company receives interest from investments and pays interest on loans, then, strictly speaking, the interest received must be shown on the credit side of the profit and loss account (because it is the

gross income from interest) and the interest paid must be entered on the debit side.

In the case of a trading company, in order to show the gross income from trading, it is necessary to disclose the figure of sales, but in the case of an engineering company it is necessary only to show the profit on contracts. If a trading company does not disclose the figure of its sales in the profit and loss account but gives therein only the amount of gross profit, it cannot be said to have complied with the above requirement of law.

*(b)* The profit and loss account shall show, arranged under the most convenient heads, the amount of gross expenditure distinguishing the expenses of the establishment, salaries and other like matters.

The gross expenditure is to be shown under appropriate heads. The details of the cost of production in the case of manufacturing and mining companies is not required. It is, however, necessary to distinguish the expenses of the 'establishment' and 'salaries'. The term 'establishment' has several meanings, but over a period of years it has been used in India as meaning salaries. As, however, according to this regulation salaries are distinct from establishment, the items that should presumably be shown under this heading are rent, rates and taxes; printing, stationery, postage, telegrams, telephone, etc; and general charges. Another point is whether wages should be shown separately or along with salaries. In practice salaries and wages are usually put together.

(c) Every item of expenditure fairly chargeable against the year's income shall be brought into account so that a just balance of profit and loss may be laid before the meeting.

This requires that the entire expenditure of the business for the period covered by the profit and loss account, whether it has been paid in cash or not, should be included therein. In ascertaining the gross amount of expenditure chargeable against the year's income, care should be taken to distinguish between capital and revenue expenditure and to capitalise expenditure the benefit of which may extend to future years.

While regulation 107 of Table A makes it obligatory for all expenditure to be brought into the profit and loss account, it does not insist on all income to be so included. It is not the law that income of every kind should be credited to profit and loss account of the year. Capital profits and profits of an exceptional nature are sometimes very rightly not credited to the profit and loss account, but are transferred direct to reserves, e. g., the Bodar Mills, Ltd , made a profit of Rs. 2,37,497 from the sale of its investments during the year ended 30th September 1943, and the directors of the Company transferred the whole amount of this profit to an Investment Reserve Fund. Similarly, if a company earns an income which is doubtful of recovery, such income should be omitted from the profit and loss account. This point is well illustrated by the following extract taken from the Directors' Report of the Belsund Sugar Co., Ltd., for the year ended 30th September 1940.

"A considerable sum is due to the Company from the Indian Sugar Syndicate, Ltd., in respect of the reduction of selling prices below basic prices in July and August 1940. In view, however, of the uncer-

tainty which still exists as to the ability of the Syndicate to meet its obligations, no credit has been taken in the Company's accounts for this outstanding asset, which cannot be finally determined pending the outcome of arbitration proceedings."

(*d*) Where any expenditure has been incurred during the year, which may in fairness be distributed over several years. the whole amount of such expenditure must be stated in the profit and loss account together with the reasons why only a portion thereof is charged against the income of the year. This, however, need not be done if the company has so decided in general meeting.

This requirement of law is of no particular significance to the shareholders. Therefore in practice almost all companies decide in general meeting to dispense with this disclosore.

II. Section 132 (3) requires some further information to be disclosed in the published profit and loss account of a company. This section reads as follows :—

"The profit and loss account shall include particulars showing the total of the amount paid whether as fees, percentages or otherwise to the managing agent, if any, and the directors respectively as remuneration for their services and, where a special resolution passed by the members of the company so requires, to the manager. and the total of the amount written off for depreciation. If any director of the company is by virtue of the nomination, whether direct or indirect, of the company, a director of any other company, any remuneration or other emoluments received by him for his own use, whether as a director of, or otherwise in connection with the management of that other company, shall be shown in a note at the foot of the account or in a statement attached thereto."

The information to be disclosed in the profit and loss account of a company under the provisions of this section may be summarised as follows :—

(*a*) The profit and loss account shall include particulars showing total of the amount paid in any form to the managing agents and the directors of the company respectively as remuneration for their services ; and where a special resolution of the company requires, the remuneration paid to the manager will also be disclosed as a separate item in the profit and loss account. The object of this disclosure in the profit and loss account is to enable the shareholders to know the cost of management and to find out whether it is reasonable or unreasonable. There has been a complaint in this country that in many cases the managing agents take the lion's share of the company's profits and give the shareholders only the crumbs.

It is obvious that only that portion of the remuneration payable to the managing agents and the directors of a company can be charged to the profit and loss account which is debitable against revenue. If any part of such remuneration is debitable to stores account and capital accounts, then such an amount cannot be debited to the profit and loss account. But the law requires that the total remuneration paid to the managing agents and the directors must be disclosed in the profit and loss account. Therefore any remuneration payable to them, which can-

not be debited to the profit and loss account will have to be shown therein merely by way of nntes.

The following extracts from the pnblished profit and loss account nt Indian companies show how the managing agents' and the directors' remuneration is to be shown :—

1. **The Titaghur Paper Mills Co., Ltd.**

**(Profit & Lnss Account for the half-year ended 30th September 1942.)**

| | Rs. | |
|---|---|---|
| To Provision for Commission to Managing Agents ... | 2,25,728 | |
| „ Allowance to Managing Agents for Office Expenses, Rent, etc. | 12,000 | |
| „ Director's Remuneratinn | 43,149 | |

2. **The Kohinnor Mills Co., Ltd.**

**(Profit & Loss Account for the year ended 31st December 1943.)**

| | Rs. | Rs. |
|---|---|---|
| Tn Auditors' & Directors' Fees | | 11,355 |
| „ Agents' Remuneration : | | |
| Office Allowance ... | 6,000 | |
| Commission on profits snbject to final adjustment in respect of excess profits tax ... | 8,15,835 | 8,21,835 |
| Cnmmission on purchases debited to Capital Expenditure | 8,527 | |
| | 8,30,362 | |

Notes.—1. The auditors' and the directors' fees should not have been mixed together. The law requires that the directors' remuneration should be shown separately.

2. The manging agents' remuneration which is debitable to Capital expenditure is shown as a note in the inner column.

3. **Punjab Natinnal Bank Ltd.**

**(Prnfit & Loss Account for the year ended 31st December 1943.)**

| | Rs. | |
|---|---|---|
| To Establishment and Provident Fund Allotment (i) ... | 29,18,052 | |
| „ Directors' Fees ... | 37,618 | |
| „ Brokerage Law Charges, Charges General, etc. (ii) | 8,38,405 | |
| „ Travelling, Telephone, Advertisement, etc. (iii) | 2,17,874 | |
| Total Rs. | | |

(i) Includes Rs 55,734 paid as salary to the General Manager and the Secretary who are also Directors

(ii) Includes Rs 1,118 earned by Directors during the year as legal fees paid to them in cases of the Bank.

(iii) Includes Rs. 5,228 paid as T. A. to the Directors and to the General Manager who is alsn a Director.

4, The Kumaran Mills Ltd.

(Profit & Loss Account for the year ended 31st December 1943.)

| | Rs. |
|---|---|
| To Managing Agents' Allowance | 12,000 |
| " Directors' Sitting Fees | 780 |
| " Managing Agents' Commission | 98,555 |
| Total Rs. | |

Note.- The total amount of commissions and allowance paid to the Managing Agents during the year ended 31st December 1943 is Rs. 1,20,663 and the E. P. T. of Rs. 57,672 is payable by them on this amount.

*(b)* The profit and loss account shall include particulars showing the total of the amount written off for depreciation It is not necessary that depreciation written off each fixed asset should be given separately in the profit and loss account only the total amount of depreciation provided for need be stated How the total amount of depreciation provided for is allocated to the different items of the Block Account is usually indicated in the balance sheet.

*(c)* If any director is nominated directly or indirectly by a company as a director of some other company, any remuneration received by such director from that other company must be shown in the profit and loss account of the company as a footnote in the profit and loss account or in a statement attached thereto. Only the aggregate amount of fees received by the nominated directors is to be given, and the amount received by each nominated director need not be given separately.

This note is sometimes included in the Directors' Report instead of in the profit and loss account; but this can be done only where the Directors' Report is signed by the same persons as are required by section 133 to sign the profit and loss account, as, for example, the following note appeared in the Directors' Report of the Burrakur Coal Co., Ltd., for the half-year ended 31st December 1940 :

"Pursuant to section 132 (3) the amounts received by the Directors of the Company by virtue of their being Directors of the subsidiary companies were as follows :- Mr. D. H. Wilmer Rs. 750 ; Mr. C. H. Heape Rs. 600."

## GROSS PROFIT AND NET PROFIT.

Theoretically speaking, the term 'Gross Profit' is the excess of sale proceeds over the cost of goods sold ; while the term 'Net Profit' stands for the excess of gross profit over the remaining expenses of the business In actual accountancy practice, however, these two terms are used in the following different senses :—

1. The term gross profit is the excess of gross income over gross expenditure, and the net profit is the balance of gross profit after making essential provisions for depreciation and taxation.

"The gross profit for the year is Rs 2,44,647, and after allowing for the reserves for depreciation and taxation, there is a net profit of Rs. 1,24,435, and a balance on this acconnt of Rs. 1,67,893." From the Directors' Report of Chumta Tea Co., Ltd, for the year ended 31st December 1942.

2. The term gross profit is nsed for the excess of gross income over gross expenditure other than interest, commission and depreciatioo; while the term net profit stands for the excess of gross profit over interest, commission and depreciation. That is to say, in arriving at the net profit taxation is not taken into account.

"During the period nnder review the company made a gross profit of Rs. 1,70,213 after meeting the manufacturing expenses, excise dnty and other expenses After allowing for interest and commission and providing Rs. 63,127 for depreciation, the accounts show a net profit of Rs. 73,842 which the Directors propose to dispose of as follows :— To Dividend at As. 4 per share for the year Rs. 12,526; to General Reserve Rs. 20,000; to Provision for iocome-tax, super-tax, etc., Rs. 30,000; and leaving to be carried forward Rs. 11 316." From the the Directors' Report of the standard Refinery and Distillery, Ltd., for the year ended 31st December 1943.

3. The term gross profit is employed in the same sense as in No. 1 above, but the use of the term net profit is dispensed with. What amounts to the net profit is simply referred to as the balaoce.

"The gross profit for the 12 months amounts to Rs. 21 78 923 to which must be added Rs. 70,343 brooght forward from last year giving a total of Rs. 2,189,266 to be dealt with. After writing off Rs. 1,05,006 for depreciation, transferring Rs. 18 000 to provision for furlough aod passage, Rs, 40,882 to general reserve, Rs 45,000 to equalisation of dividends reserve, Rs. 258,000 to reserve for renewals of plant aod machinery and Rs. 832,975 to, taxation reserve, there remains for distribution the sum of Rs. 889,404." From the Directors' Report of the British Ceyloo Corporation, Ltd., for the year ended 31st October 1943.

4. The term gross profit is not nsed, and the net profit is strnck after making provision for depreciation but before providing for taxation.

"The net profit for the year is Rs. 3,12,547, to which must be added the balance brought forward from last year Rs. 1,47,057, making in all Rs. 4,59,604 From this sum there has been set aside for taxation reserve Rs. 60,000 and for debenture redemption reserve Rs. 1 00,000 leaving an available balance of Rs 2,99.604" From the Directors' Report of the Ouchterlony Valley Estates (1938), Ltd, for the year ended 31st October 1943.

In view of the fact that the two terms 'gross profit' and 'net profit' have no generally accepted meaning in accountancy and further in view of the fact that regulation 107 of Table A does not recognise the terms gross profit and net profit, an increasing number of companies do not use these two terms in their profit and loss accounts and the directors'

reports at all. They either use simply the term 'profit' or else they call it merely the balance of the account.

It would appear, however, that if the terms gross profit and net profit are employed at all, they should be used in the sense given in No 1 above ; that is to say, the gross profit being the excess of gross income over gross expenditure, and the net profit being the excess of gross profit over the provision for depreciation and taxation. Sometimes the managing agents' commission may not be deducted from the gross profits, but is taken into account in arriving at the net profit.

**The Form of Profit & Loss Account.** Some of the principal matters, that should appear as separate items in the profit and loss account of a company, have been laid down by law, as already explained above ; but the form in which the profit and loss account is to be drawn up is left to the discretion of directors and mananging agents of companies. The form of the profit and loss account is, therefore, different in different places and in different companies. All companies do not disclose the same amount of information in their profit and loss accounts as, for instance, a mining company will not show in its published profit and loss account the details of the cost of its production. But, broadly speaking, the practice with regard to the form of the profit and loss accounts is as follows :—

(a) **The Calcutta Practice** The details of the cost of production are not disclosed in the profit and loss account, and even the stocks of raw material are omitted therefrom. The profit and loss account is usually divided into three sections as under ;

……………………………………Co , Ltd.

Profit and Loss Account for the year ended……………… …..

| | | | |
|---|---|---|---|
| Gross expenditure directly incurred in earning the gross income, e. g. :—<br>a) Stock of manufactured goods<br>b) Manufacturing expenses<br>c) Salaries and wages<br>d) Establishment<br>e) Selling expenses<br>Balance c/d | | Gross income from principal sources of trading, e. g. :—<br>a) Sales<br>b) Sundry receipts<br>c) Stock of manufactured goods | |
| Rs. | | Rs. | |
| Other expenditure, e. g.-<br>a) Interest<br>b) General charges<br>c) Directors' fees<br>d) Managing Agents' remuneration<br>e) Depreciation<br>f) Reserve for taxation<br>g) Transfer to other reserves made by directors<br>Balance c/d | | Balance b/d<br>Income from other sources, e g<br>a) Interest and dividends<br>b) Profit on sale or redemption of investments<br>c) Scrip fees<br>d) Forfeited dividends<br>e) Commission foregone by Managing Agents<br>f) Transfers from reserves | |
| Rs. | | Rs. | |

| | | | |
|---|---|---|---|
| Balance transferred to Balance Sheet | | Balance b/d. Balance b/f. from last Balance Sheet *Less* Appropriations : | |
| Rs. | | Rs. | |

It may, however, be pointed out that there is no hard and fast rule regarding the item that are shown in the first section and those that are shown in the second section. In one company a certain item may be given in the first section ; while in another it may be stated in the second The third section is, of course, used in all companies for recording the appropriations made by shareholders in general meeting.

(*b*) **The Bombay Practice.** The profit and loss accounts prepared by companies in the Western part of India are usually much more detailed ; and even the full information regarding the costs of production is included therein. The profit and loss account is prepared in two parts—the first part is the profit and loss account proper and the second part is the appropriation account. In some cases, the second part (i.e., the appropriation account) is altogether dispensed with, as the appropriations of profit are shown in detail in the balance sheet itself.

**Method of Recording Appropriations.** The power to decide how the profits of a company are to be disposed of vests in the directors, because they are the persons who are responsible for the successful working of the company. In a private business the whole of the profits may be withdrawn by the proprietors from the business ; but in a limited company the shareholders, cannot claim that all the available profits should be distributed amongst them The directors usually posses an absolute power, before recommending the amount of profits to be distributed to the shareholders, to set aside out of the profits of the company such sums as they think proper as a reserve or reserves which may be required for the purposes of the company. The practice with regard to the disposal of a company's profits is, therefore, as follows :— .

1. Transfers to reserves, if any, are made by the directors with their own authority without the consent of the shareholders, and such appropriations are shown in the profit and loss account of the year out of whose profits they are made.

2. Dividends to shareholders are to be legally recommended by the directors and are to be finally approved by the shareholders in ordinary general meetings ; and the shareholders have no right to increase the amount of dividends recommended by the directors, but they may reduce it if they so desire. In practice, however, the dividends as recommended by the directors are never reduced by the shareholders, because if they did so their own pockets would be touched.

The dividends proposed by directors out of the available profits of a particular year are not recorded in the accounts of the year out of whose profits they are to be distributed, because they are not a legal liability of the company until the ordinary general meeting of the

company has been held (and this is held during the next year) and the directors' recommendations with regard to dividends have been formally approved by the shareholders. Therefore the dividends declared are recorded in the profits and loss account of the next year.

This is the old method of accounting, and the new method of recording proposed dividends is discussed later on in this chapter.

3. The interim dividends if any, are usually declared by the directors without the sanction of the shareholders; and hence they are recorded in the profit and loss account of the year on account of whose profits they are to be distributed. The term 'interim dividend' means a dividend paid to the members of a company in anticipation of the profits of a period before the accounts of the company for that period have been prepared, audited and adopted by it at the ordinary general meeting. In other words, an interim dividend is a dividend declared at any time by the directors *between two ordinary general meetings*

4. In a few companies even the *transfers* to reserves and depreciation are recommended by the directors and are finally approved by the shareholders in ordinary general meetings. In such cases the reserve appropriations will also be recorded in the profit and loss account of the next year.

Thus, the appropriations made by the directors (which consist of depreciation and reserve transfers and interim dividends) are recorded on the debit side of the profit and loss account for the year in which they are made; while the appropriations made by the shareholders in ordinary general meetings out of the profits of a particular year are to be entered in the profit and loss account of the year in which they are made, and this may be done in any of the following three way :—

*(i)* The top section of the profit and loss account is used for recording the appropriations made in ordinary general meetings out of the profit brought forward from the last balance sheet. The appropriations are placed on the debit side and the last year's balance of profit on the credit side; and the balance of this top section, being the carry-forward, is transferred to the next section of the profit and loss account which records the income and expenditure of the current year.

*(ii)* Such appropriations are placed on the debit side of the last section of the profit and loss account or appropriation account, if any, the last year's balance of profit being placed on the credit side thereof. This is the old-fashioned method and has the disadvantage of mixing the appropriations made out of the last year's profit and those made out of the current year's

*(iii)* This is the same as the second method with the difference that the appropriations made out of the last year's profit are shown by way of deduction from the last year's profit on the credit side, instead of being placed on the debit side. This method is being increasingly employed, as it shows clearly which appropriations are out of the last year's profit and which out of the current year's

Some companies, particularly those situated on the Bombay side, do not show the shareholders' appropriations in the profit and loss account at all, but set them out in detail in the balance sheet under the heading of Profit & Loss Account.

**Proposed Dividends.** There are three methods of dealing with proposed dividends in the published accounts of a company, and these are—

1. According to orthodox accountancy, the proposed dividends (i. e., dividends recommended by the directors for the shareholders' approval) appear only in the Directors' Report; they are not shown in the profit and loss account or the balance sheet of the company for the year out of whose profits they are to be paid, since they are not legally due until they are finally sanctioned by the company in ordinary general meeting to be held next year. Therefore the balance of the profit and loss account that is included in the balance sheet is without giving effect to such proposed dividends; and the balance sheet therefore does not show the current position of the company, as the payment of the proposed dividends will involve a payment of the amount recommended from the cash balance of the company—a fact which is not apparent from an inspection of the balance sheet.

2. According to modern accountancy practice, in order to make the balance sheet more informative and self-contained, some companies are now giving effect to the proposed dividends in the profit and loss account and the balance sheet, though it must be borne in mind that the directors have not the power to declare these dividends but they may only recommend to the shareholders to do so. In practice, however, the shareholders always follow the suggestions of their directors in this respect, as they have no power to declare a dividend in excess of that recommended and they are obviously not likely to propose a resolution that a lower rate should be paid.

This method has the distinct advantage of showing the true financial position of the company at a glance. When this method is adopted, the proposed dividends are recorded in the profit and loss account as if they were duly declared, and their amount is set out under the current liabilities in the balance sheet, e g.—

**The India United Mills, Ltd.**

Appropriation Account for the year ended 31st December 1943.

| | Rs. | Rs | | Rs |
|---|---|---|---|---|
| To Depreciation Account | | 30,00,000 | | |
| ,, General Reserve ... | | 30,00,000 | By Balance b/f. from 1942 ... | 13,32,148 |
| ,, Old Employee's Pension and Gratuity Fund ... | | 1,00,000 | By Balance from Profit and Loss Account | 94,68,549 |
| ,, Provision for Proposed Dividends: | | | | |
| Dividend at annas fifteen and Bonus at annas five for Ordinary Shares of Rs. 10 each, free of income tax ... | 25,00,000 | | | |
| Dividend at annas three and Bonus at annas two for Deferred Shares of Re. 1 | | | | |

| | | | |
|---|---|---|---|
| each, free of income-tax ... | 15,62,500 | 40,62,500 | |
| „ Balance carried to Balance Sheet ... | | 6,38,197 | |
| | | Rs. 1,08,00,697 | Rs. 1,08,00,697 |

A separate item called "Provision for Proposed Dividends Rs. 40,62,500" appears on the liabilities side of the Company's Balance Sheet as on 31st December 1943

3. Between the first (old method) and the second (ultra-modern) method there is the third method by which the proposed dividends are not debited to the profit and loss account nor are they shown as a liability in the balance sheet But neither is all mention of the proposed dividends omitted from the published accounts. This consists of setting out in an indented note on the debit side of the profit and loss account the amount of the proposed dividends, and the effect which the payment thereof will have on the carry-forward. Thus the effect of the payment of the dividends, if they are agreed to at the ordinary general meeting, is clearly set out for all to see, but they are not actually deducted from the carry forward and the assumption is not made that the meeting must necessarily follow the directors in agreeing to their recommended dividends.

The Council of the Institute of Chartered Accountants in England and Wales has made a series of recommendations on accounting principles. These provide an authoritative indication of what is regarded as "the best practice". Given below is their recommendation in regard to the inclusion of proposed profit appropriations in the accounts of a company :—

"Although certain appropriations of profits, including dividends recommended by directors, are subject to subsequent confirmation by shareholders, the inclusion of all appropriations in the accounts shows the amount which will be required for distribution to the shareholders and completes the accounts for the financial year by showing the results of trading and their application in one account. This course avoids the inclusion in the accounts of the next period of appropriations which were set out in the directors' report for the previous period and have already been dealt with and disposed of. Also, it facilitates the linking up of the accounts from one period to another, the balance carried forward to the following period being clearly shown in the accounts of each year.

"Recommendation—Provision should be made in the books and in the Annual Accounts for proposed profit appropriations, those subject to confirmation by shareholders being so described. Provision for dividends should be shown as a separate item in the Balance Sheet."

In order to illustrate what has been discussed above in this chapter; a number of actual published profit and loss accounts of Indian companies engaged in different industries are appended.

1. **The Dalhousie Jute Co., Ltd.**

Profit & Loss Account for the half-year ended 31st March 1941

| | Rs. | Rs. | | Rs. | Rs. |
|---|---|---|---|---|---|
| To Stock on 30-9-40 | | 12,95,128 | By Gunny Sales ... | | 28,60,190 |
| „ Gunny Purchases ... | | 77,727 | „ Stock on 31-3-41 ... | | 9.02,536 |
| „ Mfg. Expenses ... | | 15,02,988 | | | |
| „ Salaries & Wages ... | | 4,50,464 | | | |
| „ Establishment Expenses ... | | 30,636 | | | |
| „ Brokerage on Sales ... | | 14,454 | | | |
| „ Balance c/d ... | | 3,91,329 | | | |
| | Rs. | 37,62,726 | | Rs. | 37,62 726 |
| To Law Charges ... | | 100 | By Balance b/d ... | | 3,91,329 |
| „ Provision for Mg. Agents' Commission ... | | 21,102 | „ Interest on Investments ... | | 37,768 |
| „ Mg. Agents Allowance to cover Establishment, Rent etc. ... | | 19.500 | „ Transfer from Equalisation of Dividend Fund ... | | 15,000 |
| „ Directors Remuneration ... | | 4,650 | | | |
| „ Interest ... | | 1 277 | | | |
| „ Forfeited Dividends ... | | 1,125 | | | |
| „ Provision for Taxation ... | | 1,97,216 | | | |
| „ Depreciation ... | | 44,863 | | | |
| „ Balance c/d ... | | 1,54,264 | | | |
| | Rs. | 4,44,097 | | Rs. | 4,44,097 |

| | | | | | |
|---|---|---|---|---|---|
| To Dividend paid on Preference Shares for the half-year ended 30-9-1940 | 52,500 | | By Balance at 1-10-1940 ... | | 1,78,019 |
| ,, Dividend paid on Ordinary Shares for the half-year ended 30-9-1940 ... | 1,12,500 | 1,65,000 | ,, Balance b/d ... | | 1,54,264 |
| ,, Balance carried to B/S. ... | | 1,67,283 | | | |
| | Rs. | 3,32 283 | | Rs. | 3,32,283 |

2.

**The Burraker Coal Co., Ltd.**

Profit & Loss Account for the half-year ending 31st December 1940.

| | Rs. | Rs. | | Rs. | Rs. |
|---|---|---|---|---|---|
| To Stock on 30-6-40 ... | 1,37,901 | | By Sales ... | | 24,07,594 |
| ,, Coal and Coke in Transit ... | 2,417 | 1,40,318 | ,, Bye-Products Sales ... | | 1,41,486 |
| ,, Production Account ... | | 15,63,941 | ,, Income from Royalties and Rents ... | | 61,230 |
| ,, Coal purchased ... | | 3,19,944 | ,, Stock on 31-12-40 ... | 1,13,983 | |
| ,, Freight and Delivery ... | | 1,84,914 | ,, Coal in Transit ... | 1,109 | 1,15,092 |
| ,, Salaries ... | | 91,251 | | | |
| ,, Establishment ... | | 46,866 | | | |
| ,, Charges General ... | | 19,490 | | | |
| ,, Law charges ... | | 4,604 | | | |
| Road Cess ... | | 3,792 | | | |
| Balance c/d ... | | 3,50,282 | | | |
| | | 27,25,402 | | | 27,25,402 |

| | | | | | |
|---|---|---|---|---|---|
| To Directors Fees ... | 1,120 | | By Balance b/d ... | | 3,50,282 |
| ,, Directors Comn. ... | 2,226 | | ,, Scrip Fee ... | 27 | |
| ,, Provident Fund Coutribution | 8,102 | 11,448 | ,, Gnarantee Comn. ... | 1 | |
| ,, Mg. Agents' Remuneration (includes provision of Calcutta office accommodation and staff) ... | | 1,10,555 | ,, Interest ... | 48,537 | |
| ,, Provision for Income and Super Taxes ... | | 68,350 | ,, Interest on Govt. Secnrities... | 5,599 | |
| ,, Depreciation ... | | 1,10 795 | ,, Dividend on Investments ... | 73 | |
| ,, Balance c/d ... | | 1,57,107 | ,, Profit on Sale of Investments | 5,174 | 59,411 |
| | | | ,, Sndry Revenue ... | | 2,627 |
| | | | ,, Salami ... | | 7,600 |
| | | | ,, Forfeited Dividends ... | | 3,335 |
| | | | ,, Equalisation of Dividend Reserve ... | | 20,000 |
| | | | ,, Commission foregone by Mg. Agents ... | | 15,000 |
| | | 4,58,255 | | | 4,58,255 |
| To Dividends ... | | 2,22,563 | By Balance as at 30-6-1940 ... | | 2,93,930 |
| ,, Balance (carried to B/S.) ... | | 2,28,474 | ,, Balance b/d ... | | 1,57,107 |
| | | 4,51 037 | | | 4,51,037 |

*Notes*—1. Details of the cost of production are not disclosed.

2. The dividends paid out of the previous year's profit are put on the debit side of the last section of the Profit and Loss Account.

3.

**The Searsole Coal Co., Ltd.**

Profit & Loss Account for the year ended 31st January 1941.

| | Rs. | Rs. | | Rs. | Rs. |
|---|---|---|---|---|---|
| To Stock of Coal on 1-2-40 ... | | 10,847 | By Coal Sales ... | | 91,778 |
| " *Calcutta* Expenses (including Directors' Fees Rs. 224) ... | | 1,472 | " Stock of Coal on 31-1-41 ... | | 10,426 |
| " Colliery Expenses (including Salaries and Wages Rs. 7830) | | 67,670 | " Sundry Receipts ... | | 84 |
| " Managing Agents' Allowance including Allowance for Staff | | 9,600 | | | |
| " Gross Profit for the year c/d | | 12,699 | | | |
| | | Rs. 1,02,288 | | | Rs. 1,02,288 |
| To Managing Agents' Commission | | 1,029 | By Gross Profit for the year b/d | | 12,699 |
| " Depreciation— | | | " Interest ... | | 968 |
| On Machinery & Plant ... | 1,285 | | " Transfer Fees ... | | 51 |
| " Development ... | 294 | | | | |
| " Buildings ... | 422 | | | | |
| " Furniture ... | 206 | | | | |
| " Electric Installation ... | 3,270 | 5,477 | | | |
| To *Net Profit for the year c/d.* ... | | 7,212 | | | |
| | | Rs. 13,718 | | | Rs. 13,718 |
| To Balance c/f ... | | 37,075 | By Balance b/f. from previous year | 36,113 | |
| | | | *Less* Dividend on 50000 Shares of Rs. 2-8-0 each at 5% (free of Income-Tax) for the year ended 31-1-40 ... | 6,250 | 29,863 |
| | | | Net Profit for the year b/d ... | | 7,212 |
| | | Rs. 37,075 | | | Rs. 37,075 |

4.

**The Betjan Tea Co., Ltd.**

Profit & Loss Account for the year ended 31st December 1940

| | Rs. | Rs | | Rs. | Rs. |
|---|---|---|---|---|---|
| To Salaries and Wages ... | 1,02,738 | | By Proceeds of Crop :— | | |
| ,, Establishment ... | 1,228 | | 4,84,399 lbs. sold ... | 3,64,701 | |
| ,, Cultivation ... | 10,461 | | *Less* Sale Charges | 5,113 | 3,59,588 |
| ,, Labour ... | 2 503 | | 13,560 lbs. Stock valued at below current market rate ... | 3,390 | |
| ,, Crop ... | 43,829 | | *Less* Sale Charges ... | 90 | 3,300 |
| ,, Repairs and Upkeep of Buildings, Roads and Bridges ... | 7,939 | | | | |
| ,, Repairs and Upkeep of Machinery ... | 2,595 | | | | 3,62,888 |
| ,, Land Rent and Taxes ... | 4,919 | | *Less* Shipping Charges incnrred by Calcutta Office. ... | | 815 |
| ,, General Stores ... | 1,623 | | 507 lbs. short on reweighment .. | | |
| ,, General Charges ... | 6,248 | | | | |
| ,, Legal Expenses ... | 127 | 1,84,210 | | | |
| ,, Calcutta Charges (including Directors' Fees Rs. 384) ... | 1,110 | | 4,98,466 Total Crop for Season 1940 | | 3.62,073 |
| ,, Managing Agents' Commission, and Office Allowance ... | 12,979 | 14,089 | *Less* Cost of Export Quota brought ... | 54,360 | |
| | | | Deduct Value of Internal Quota sold ... | 761 | 53,599 |
| | | | | | 3,08,474 |
| ,, Balance being Gross Profit for the year c/f. ... | | 1,11,013 | By Valne of Sweepings ... | | 455 |
| | | | ,, Miscellaneous Receipts ... | | 383 |
| | Rs. | 3,09,312 | | Rs. | 3.09,312 |

| | | | | | |
|---|---|---|---|---|---|
| To Manager's and Assistants' Commission ... | | 11,223 | By Balance b/f ... | | 1,11,013 |
| " I. T. and S. T. ... | | 16,556 | " Interest ... | | 2,888 |
| " Provident Fund ... | | 1,565 | " Scrip Fee ... | | 1 |
| " Net Profit c/d ... | | 84,558 | | | |
| | Rs. | 1,13,902 | | Rs. | 1,13,902 |
| To Balance c/d ... | | 1,28,609 | " By Balance b/f from previous year ... | 1,08,022 | |
| | | | *Add* Adjustment Season 1939 ... | 29 | |
| | | | | 1,08,051 | |
| | | | *Less* Dividend for 1939 on 32,000 Ordinary Shares of Rs. 10 each at 20% free of income-tax ... | 64,000 | 44,051 |
| | | | " Net Profit for 1940 b/d ... | | 84,558 |
| | Rs. | 1,28,609 | | Rs. | 1,28,609 |

*Note* *The use of the terms gross profit and net profit in this Profit & Loss Account.*

5.

**The Ryam Sugar Co., Ltd**

Profit & Loss Account for the year ended 30th June 1940.

| | Rs. | Rs. | | Rs. | Rs. |
|---|---|---|---|---|---|
| To Stock of Sugar (Less Sugar Excise Duty) and Molasses as on 1—7—1939 ... | | 1,93,705 | By Sale Proceeds of Sugar and Molasses ... | 8,43,321 | |
| | | | " Sundry Receipts ... | 8,773 | 8,52,094 |

| | | | | | | |
|---|---|---|---|---|---|---|
| To Raw Material and Mfg. ... | | 17,81,909 | | " Stock of Sugar (Less Sugar Excise Duty) and Molasses as on 30—6—1940 ... | | 16,08,026 |
| " Bihar Govt. Cane Cess ... | | 62,666 | | | | |
| " Salaries and Wages ... | | 1,77,829 | | | | |
| " Sugar Excise Duty | 2,89,053 | | | | | |
| *Less* Payable on Stocks | 2,15,223 | 73,830 | | | | |
| " Marketing ... | | 7,481 | | | | |
| " Insurance ... | | 22,189 | | | | |
| " Establishment ... | | 21,212 | 21,47,116 | | | |
| " Balance c/d ... | | | 1,19,299 | | | |
| | | Rs. | 24,60,120 | | Rs. | 24,60,120 |
| To Directors' Fees ... | | 1,800 | | By Balance b/d... ... | | 1,19,299 |
| " Audit Fee ... | | 1,000 | | " Dividends and Interest ... | | 858 |
| " Contribution to War Purposes Fund .. | | 2,000 | | | | |
| " Interest — | | 22,832 | | | | |
| " Mortgage Debenture Bond Interest .. | | 26,250 | | | | |
| " Mg Agents Remun ... | | 18,039 | | | | |
| " Taxation Reserve for Fiscal year 1941–42 .. | | 2,000 | 73 921 | | | |
| " Balance c/d ... | | | 46,236 | | | |
| | | | Rs.1,20,157 | | | Rs.1,20,157 |
| To Balance as on 1—7—1939 ... | | | 2,47,120 | By Balance b/d ... | | 46,236 |
| | | | | " Balance as per B/S. ... | | 2,00,884 |
| | | | Rs 2,47,120 | | | 2,47,120 |

6.

**The Muir Mills Co., Ltd.**
Profit & Loss Account for the year ended 31st December 1940

| | Rs. | Rs. | | | Rs. | Rs. |
|---|---|---|---|---|---|---|
| To Mfg. Expenses ... | | 58,93,585 | By Turnover Less Selling Commission and Discounts ... | | | 95,56,853 |
| Establishment Charges :— | | | Rents received ... | | | 1,460 |
| Salaries and Wages ... | 21,24,099 | | Transfer Fees ... | | | 72 |
| Rent, Rates, Taxes, Insurance and other General Charges ... | 1,15,229 | 22,39,328 | | | | |
| Interest paid *less* received | | 26,931 | | | | |
| Taxation ... | | 6,25,000 | | | | |
| Directors Fees ... | | 4,800 | | | | |
| Depreciation ... | | 2,50,000 | | | | |
| Pension and Gratuity Fund | | 20,000 | | | | |
| Balance c/d ... | | 4,98,741 | | | | |
| | | 95,58,385 | | | | 95,58,385 |
| To Ad-interim Dividends for half-year ended 30-6-1940 | | 1,95,000 | By Balance at 31-12-1939 after payment of Ad-interim dividends ... | | 3,66,154 | |
| Balance carried to B/S ... | | 4,29,895 | *Less* Final Dividend on Preference Shares for 1939 | 45,000 | | |
| | | | Final Dividend on Ordinary Shares for 1939 | 1,50,000 | | |
| | | | Bonus of Rs. 1/8 per Ordinary Share for 1939 | 45,000 | 2,40,000 | 1,26,154 |
| | | | Balance b/d ... | | | 4,98,741 |
| | | Rs.6,24,895 | | | | Rs.6,24,895 |

*Note* —No Stocks of any kind are disclosed in this Profit & Loss Account. The Stocks of Raw Materials are included in Manufacturing Expenses, and those of Finished Goods in the Turnover.

7.

**The Elgin Mills Co., Ltd.**
Profit & Loss Account for the half-year ended 30th September 1940

| | Rs. | Rs. | | Rs. | Rs. |
|---|---|---|---|---|---|
| To Stock of manufactured goods on 1-4-1940 ... | | 17,82,101 | By Sales ... | | 60,90,397 |
| " Raw Materials and Manufacturing ... | 36,91,380 | | " Rent Collections ... | | 4,062 |
| " Salaries and Wages ... | 10,67,764 | | " Stock of manufactured goods on 30-9-40 ... | | 13 59,412 |
| " Marketing ... | 60,506 | | | | |
| " Insurance ... | 26,175 | | | | |
| " Establishment and other Expenses ... | 25,421 | | | | |
| " Welfare Expenses ... | 15,379 | 48,86,625 | | | |
| " Balance c/d ... | | 7,85,145 | | | |
| | Rs. | 74,53,871 | | Rs. | 74,53,871 |
| To Directors' Fees ... | 500 | | By Balance b/d ... | | 7,85,145 |
| " Audit Fee ... | 1,250 | | " Interest Received ... | | 17,963 |
| " Interest Paid ... | 70,538 | | | | |
| " Debenture Interest ... | 35,000 | | | | |
| " Mg. Agents' Remun. ... | 54,172 | | | | |
| " Contribution to War Purposes Fund ... | 10,000 | | | | |
| | | 1,71,460 | | | |
| " Taxation Reserve ... | | 2,10,000 | | | |
| " Deb-Sinking Fund ... | | 25,000 | | | |
| " Depreciation ... | | 1,75,000 | | | |
| " General Reserve ... | | 47,145 | | | |
| " Balance c/d ... | | 1,74,503 | | | |
| | Rs. | 8,03,108 | | Rs. | 8,03,108 |

| | | | | | |
|---|---|---|---|---|---|
| *To* Balance as per Balance Sheet | | 2,28,434 | By Balance b/d ... | | 1,74,503 |
| | | | „ Balance from last Account | 2,02,931 | |
| | | | *Less* Dividends for the half-year ended 31-3-40 | 1,49,000 | 53,931 |
| | Rs. | 2,28,434 | | | 2,28,434 |

8. **The Assam Saw *Mills* and Timber Co., *Ltd.***

Revenue Account for the year ended 30th September 1940

| | Rs. | | Rs. |
|---|---|---|---|
| To Stock as on 30-9-39 ... | 71,274 | By Sales ... ... | 11,00,642 |
| „ *Mfg.* and other Expenses ... | 5,26,782 | „ Stock as on 30-9-40 ... ... | 1,20,036 |
| „ Wages and Salaries ... | 3,27,132 | | |
| „ Calcutta Expenditure ... | 9,284 | | |
| „ Balance being gross profit transferred to P. & L. a/c ... | 2,86,206 | | |
| Rs. | 12,20,678 | Rs. | 12,20,678 |

Profit & Loss Account for the year ended 30th September 1940

| | Rs. | Rs. | | Rs. | Rs. |
|---|---|---|---|---|---|
| To Dividend paid at As. 2 per share (free of Income-Tax) on 2,95,056 Ordinary Shares | | 36,882 | By Balance as on 30-9-39 | | 42,367 |
| „ Balance c/d ... | | 5,485 | | | |
| | | 42,367 | | | 42,367 |
| To Law charges ... | 24 | | By Balance b/d ... | | 5,485 |
| „ Mg. Agents Allowance ... | 18,000 | | „ Scrip Fees — | | 19 |
| „ „ „ Commission ... | 23,098 | | „ Balance transferred from Revenne % ... | | 2,86,205 |
| „ Deb-Interest ... | 20,444 | | „ Profit on sale of Steam Launch "Ibis" ... | | 900 |
| „ Deb. Trustees Fees — | 500 | | | | |
| „ Overdraft Ioterest ... | 4,265 | | | | |
| „ Directors Fees ... | 1,800 | | | | |
| „ Directors Commission ... | 4,620 | | | | |
| „ Workmen's Compensations | 210 | 72,961 | | | |
| „ Depreciation — | | 77,636 | | | |
| „ Live Stock Written off ... | | 8,108 | | | |
| „ Reserve for Discounts ... | | 10,000 | | | |
| „ Deb. Redemption Fund ... | | 40,000 | | | |
| „ Balance carried to B/S. ... | | 83,904 | | | |
| | Rs. | 2,92,609 | | | 2,92,609 |

9.

**The Indian Galvanizing Co. (1926) Ltd.**

Profit & Loss Account *for the year* ended 31st December 1940

| | Rs. | Rs. | | Rs. | Rs. |
|---|---|---|---|---|---|
| To Mfg. and other charges ... | 79,493 | | By Gross Income ... | | 9,30,665 |
| " Salaries and Wages ... | 2,27,169 | | " Interest ... | | 1,963 |
| " Establishment ... | 17,992 | | | | |
| " Mg. Agents' Allowance and Commission ... | 52,037 | | | | |
| " Directors' Fees and Commission ... | 12,661 | 3,89,352 | | | |
| " Balance c/d ... | | 5,43,276 | | | |
| | Rs. | 9,32,628 | | Rs. | 9,32 628 |
| To Block Depreciation ... | 1,09,989 | | By Balance b/d ... | | 5,43,276 |
| " Provision for Taxation ... | 2,77 000 | 3,86,989 | | | |
| " Balance c/d ... | | 1,56,287 | | | |
| | Rs. | 5,43,276 | | Rs. | 5,43,276 |
| To Amount *transferred* to Reserve — | 50,000 | | By Balance as at 31-12-1939 | 90,556 | |
| " Amount transferred to Stock Reserve | 16,844 | 66,844 | *Less* Dividend of 15% per annum for the year ended 31-12-1939 ... | 61,576 | 28,980 |
| " Balance carried to B/S. ... | | 1,18,423 | " Balance b/d ... | | 1,56,287 |
| | Rs. | 1,85,267 | | | 1,85,267 |

10.

**Smith, Staoistreet & Co., Ltd.**
Profit & Loss Account for the year ended 30th June 1940

| | Rs | Rs. | | Rs. | Rs. |
|---|---|---|---|---|---|
| To Dividend for the year to 30-6-1939 on the 10% Preference Shares, free of Income-Tax ... | 50 000 | | By Balance as per last account | | 1,22,326 |
| ,, Dividend for the year to 30-6-1939 on the Ordinary Shares at four annas per Share (100% p. a) free of Income-Tax ... | 25,000 | 75,000 | | | |
| ,, Balance c/d ... | | 47,326 | | | |
| | Rs. | 1,22,326 | | Rs. | 1,22,326 |
| To Depreciation ... | | 12,520 | By Balance b/d ... | | 47,326 |
| ,, P. F. Contribution ... | | 3,370 | ,, Balance from Revenue Account ... | | 1,32,303 |
| ,, Provision for Taxation ... | | 46,800 | ,, Manufacturing Account ... | | 27,759 |
| ,, General Reserve ... | | 379 | ,, Sundries ... | | 534 |
| ,, Bank Interest .. | | 1,579 | | | |
| ,, Interest General ... | | 55 | | | |
| ,, Directors' Fee ... | | 50 | | | |
| ,, Difference in Exchange ... | | 568 | | | |
| | | 65,321 | | | |
| ,, Balaoce transferred to Balance Sheet ... | | 1,42,601 | | | |
| | Rs. | 2,07,922 | | Rs. | 2,07,922 |

*Notes.*—1. The appropriations made out of the previous year's profit are shown at the top of the Profit and Loss Account.
2. This Profit and Loss Account is too abridged. Even the figure of sales is not disclosed, which should have been done according to law.

11.

**The Nutan Mills, Ltd.**

Profit & Loss Account for the year ended 31st December 1940

| | Rs. | Rs. | | Rs | Rs. |
|---|---|---|---|---|---|
| To Cotton consumed ... | | 12,85,749 | By Yarn ... | 10,660 | |
| " Yarn ... | | 87,983 | " Cloth ... | 31,43,271 | |
| " Salaries, Wages, Stores, etc. | 10,84,991 | | " Waste ... | 29,092 | 31,83,023 |
| " Fuel ... | 1,30,180 | | " Miscellaneous Income ... | | 3,848 |
| " Interest ... | 1,05,824 | | " Share Transfer Fees ... | | 56 |
| " Insurance ... | 8,557 | | | | |
| " Rent, Taxes etc. ... | 25,228 | | | | |
| " Brokerage ... | 15,972 | | | | |
| " Auditors' Fee ... | 400 | | | | |
| " Directors' Fees ... | 540 | | | | |
| " Building and Machinery Repairs ... | 26,110 | 13 97,802 | | | |
| " Agents' Commissions ... | | 1,09,308 | | | |
| " Profit (without deducting depreciation) ... | | 2,06,085 | | | |
| | Rs. | 31,86,927 | | Rs. | 31,86,927 |

*Notes.*—1. No stocks of any kind have been disclosed in this Profit and Loss Account, because they have been adjusted into Cotton, Yarn, Cloth, Waste and Stores Accounts.

2. The appropriations of profit, instead of being shown in the Profit and Loss Account, are given in the Balance Sheet.

THE ASSOCIATED CEMENT

Profit and Loss Account for the

| Previous year. | | | |
|---|---|---|---|
| 10,62,282 | To Stocks of Clinker and Cement on 1—8—1939 ... ... | | 14,09,389 |
| 34,19,251 | ,, Salaries and Wages ... | 34,87,131 | |
| 2,749 | *Less*—Recoveries ... ... | 1,045 | |
| 34,16,502 | | | 34,86,086 |
| | ,, Operation Expenses:— (after deducting salaries & wages) | | |
| 1,15,10,205 | Coal, Bags, Raw Materials and Stores ... ... | 1,07,59,313 | |
| 2,66 202 | Water, Electricity and other Charges ... ... | 2,51,230 | |
| 2,84,117 | Factory Expenses: (Comprising Laboratory Expenses, Medical Expenses, Office Expenses, Travelling Expenses, General Expenses, Rent, Rates & Taxes, Workmen's Compensation Workmen's Welfare Expenses etc.) | 3,16,402 | |
| 1,30,60,524 | | | 1,13,26,945 |
| 10,47,874 | ,, Repairs and Maintenance (after deducting Salaries and Wages) | | 8,53,016 |
| 42,325 | ,, Insurance ... ... | | 39,371 |
| 5,11,240 | ,, Royalties and Duties ... | | 4,55,869 |
| 1,13,78,804 | ,, Freight & Transportation Charges on Cement (including Marine Insurance and Contribution to the Insurance Fund) ... | | 1,00,76,478 |
| 29,44,571 | ,, Commissions, Discounts, Rebates etc., on Cement Sales (including Sales Tax) ... | | 24,65,428 |
| | ,, Advertising & Selling Expenses | 4,66,073 | |
| 3,59,416 | *Less*—Recoveries ... | 65,347 | 4,00,726 |
| | ,, Establishment Expenses:- Bombay and other offices after deducting Salaries & wages) | | |
| 53,710 | Rent, Rates and Taxes ... | 54,563 | |
| 66,807 | Printing and Stationery, Postage Telegrams, Telephones etc. ... | 79,609 | |
| 1,20,639 | General Expenses: (Comprising Travelling Expenses office Furniture Maintenance, Collections and Exchange, Donations, General Charges etc.) ... | 1,95,061 | |
| 2,41,156 | | | 3,29,233 |
| 1,08,120 | ,, Cost of Dismantling Buildings and Machinery and Railway Freight and Erection Charges on Machinery Transfer — — | | 1,56,799 |

COMPANIES, LIMITED.

year ended 31st July 1940.

| Previous year. | | | |
|---|---|---|---|
| 4,08,39,920 | By Cement Sales (including Cement used at works amounting to Rs. 31,929) ... ... | | 3,79,47,075 |
| 14,09,389 | " Stocks of Clinker and Cement on 31—7—1940 ... ... | | 21,18,444 |
| | " Sale of Power, Water, Stores, Ballast, Gypsum, Scrap, *Empties etc.* ... ... | 1,61,981 | |
| | *Less*—Outward Freight ... | 431 | |
| 1,40,767 | | | 1,61,550 |
| ... | " Share of the Patiala Cement Co., Ltd. in the Apportionment of C. A. I., Publicity and Head Office Establishment Charges | | 52,302 |
| | " Interest on Investments | 22,829 | |
| | *Less*—Income-Tax ... ... | 3,591 | |
| 69,358 | | | 19 238 |
| 47,493 | " Other Interest .. ... | | 1,32,865 |
| ... | " Interest on Workmen's Welfare and Benefit Fund Investments | 710 | |
| | *Less*-Transferred to Workmen's Welfare and Benefit Fund ... | 710 | |
| | | | ... |
| 30,880 | " Dividend on Shares ... | | 1,50,000 |
| 21,216 | " Transfer Fees etc. .. ... | | 37,869 |
| 54,069 | " Miscellaneous Receipts ... | | 42,038 |
| 4,26,13,092 | | Rs. | 4,06,61,381 |

| | | | |
|---|---|---|---|
| 70,274 | " Buildings, Machinery, Rolling Stock, Motor-Cars, Furniture etc. written off ... ... | | 85,220 |
| 40,286 | " Loss on Sale of Investments ... | | 13,484 |
| 11,419 | " Legal Expenses ... ... | | 10,403 |
| 1,30,628 | " Prospecting Expenses written off | | 1,69,528 |
| | " Unallocated Expenditure on New works written off ... | | 1,00,000 |
| 45,009 | " Directors' Fees and Travelling Expenses ... ... | | 34,705 |
| 12,500 | " Auditors' Fees (including Works' inspection) ... ... | | 13,800 |
| 25,538 | " Interest on Debenture Loan ... | | 20,209 |
| 5,700 | " Other Interest ... ... | | 52,562 |
| 370 | " Bad Debts ... ... | | 38 |
| 1,80,376 | " Company's Contribution to the Provident Fund ... ... | | 1,66,884 |
| 6,97,247 | " Managing Agents' Commission | | 7,15,425 |
| 38,55,463 | " Provision for Depreciation (including Rs. 24,958 written off on revalution of Loose Plant & Tools) . .. | | 37,00,000 |
| 10,37,000 | " Provision for Income-tax and Super-tax .. ... | | 8,04,000 |
| 33,28,468 | " Net Profit carried to App. Account | | 37,75,783 |
| 4,26,13,092 | | Rs. | 4,06,61,381 |

*Note.*—Remuneration received for their own use by Directors who were appointed to be the first directors of The Patiala Cement Co. Ltd, when that Company was promoted and its directorate settled to Rs. 1,550 during the year.

THE ASSOCIATED CEMENT

Profit and Loss Appropriation Account

| Previous year. | | | |
|---|---|---|---|
| 1,00,400 | To Provision for Redemption of Debentures ... ... | 1,05 919 | |
| | *Less* Recovered from the Patiala Cement Co., Ltd. ... | 19,988 | |
| | | | 86,931 |
| 1,50,000 | To Bonus to Employees...... | | 1,70,000 |
| 40,00,992 | " Balance carried to Balance Sheet | | 39,92,739 |
| 42,51,392 | | Rs. | 42,49,670 |

COMPANIES, LIMITED.

at 31st July 1940.

| Previous year. | | | |
|---|---|---|---|
| 44,50,029 | By Balance as per last year's Account | 40,00,992 | |
| | *Less* Dividend at Rs. 5 per share, Free of Income-Tax, for the | | |
| 35,27,105 | year ended 31–7–1939 ... | 35,27,105 | |
| 9,22,924 | | | 4,73,887 |
| 33,28,468 | " Balance brought down from Profit and Loss Account ... ... | | 37,75,783 |
| 42,51,392 | | Rs. | 42,49,670 |

THE BOMBAY DYEING AND MANU

Profit and Loss Account for the year

| | Rs. | Rs. |
|---|---|---|
| To Stock on hand on 1st January, 1940:— | | |
| Cotton, cloth, yarn and waste ... ... | 40,54,429 | |
| Chemicals, stores, oil, fuel and coal ... | 8,78,001 | |
| | | 49,32,430 |
| „ Purchases of:— | | |
| Cotton and yarn ... ... ... | 85,57,598 | |
| Chemicals, stores, oil fuel and coal ... | 21,37,901 | |
| | | 1,06,95,499 |
| „ Electric energy ... ... ... | | 5,96,700 |
| „ Working and office establishment charges ... | | 47,13,119 |
| „ Medical and Maternity Benefit expenses ... | | 41,015 |
| „ Municipal, Property and Land taxes ... | | 1 23,007 |
| „ Commission on sales of yarn and cloth ... | | 1,28,440 |
| „ Company's contributions to recognised provident fund ... ... ... | | 84,665 |
| „ Fire, workmen's compensation and cash-in-transit insurance ... ... ... | | 78,109 |
| „ Ground rent ... ... ... | | 21,526 |
| „ Printing, stationery, telegrams, water charges and sondry expenses ... ... | | 2,06,502 |
| „ Building and machinery repairs ... ... | | 16,084 |
| „ Directors' fees ... ... ... | | 7,500 |
| „ Auditors' fees ... ... ... | | 6,000 |
| „ Agents' remuneration ... ... | | 1,80,216 |
| | | 2,18,30,812 |
| „ Depreciation:— | | |
| On Buildings ... ... ... | 1,60,000 | |
| „ Machinery ... ... ... | 4,25,000 | |
| „ Motor Lorries ... ... ... | 1,803 | |
| | | 5,86,803 |
| „ Provision for Income-tax and Super-tax ... | | 2,50,000 |
| | | 2,26,67,615 |
| „ Balance, carried down ... ... | | 6,53,896 |
| | Rs. | 2,33,21,511 |

Appropriation Account for

| | | |
|---|---|---|
| To Dividends and Bonus ... ... | | 8,78,430 |
| „ Balance, carried to Balance Sheet ... | | 7,54,994 |
| | Rs | 16,33,424 |

FACTURING COMPANY LTD.
ended 31st December 1940.

| | Rs. | Rs |
|---|---|---|
| By Proceeds of cloth, yarn and waste and dyeing (after deductions of trade discount, brokerage and sahi) ... ... ... | | 1,89,02,959 |
| ,, Interest on Investments ... ... | 2,78 102 | |
| *Less*—Income-tax deducted ... ... | 22,661 | |
| | 2,55,441 | |
| *Add*—Other interest received ... ... | 15,821 | |
| | 2,71,262 | |
| *Less*—Interest paid out ... .. | 35,958 | |
| | | 2,35,304 |
| ,, Chawl rent ... ... ... | | 20,750 |
| ,, Share transfer fees .. ... ... | | 962 |
| ,, Stock on hand on 31st December, 1940:— | | |
| Cotton, cloth, yarn and waste ... ... | 30,55 225 | |
| Chemicals, stores, oil fuel and coal ... | 11,06,311 | |
| | | 41,61,536 |
| | Rs. | 2,33,21,511 |

the year ended 31st December 1940.

| | | |
|---|---|---|
| By Balance of Profit brought forward from last year | - | 9,79,528 |
| ,, Balance, brought down ... .. | | 6 53,896 |
| | Rs | 16,33,424 |

14. THE GOLD MOHUR

Profit & Loss Account for the year

| 1939 Rs. | | Rs. | Rs. |
|---|---|---|---|
| | To Cotton :— | | |
| | Opening stock ... | 5,81,319 | |
| | Purchased during the year ... | 19,64,058 | |
| | | 25,45,377 | |
| | *Less* Closing stock ... | 5,31,907 | 20,13,470 |
| 16 30,786 | ,, Stores, machinery Spares, Dyes and Chemicals Opening stock ... | 2,90,928 | |
| | Purchased during the year ... | 6,89,840 | |
| | | 9,80,768 | |
| | *Less* Closing stock ... | 4,11,466 | |
| 4,45,597 | | | 5,69,302 |
| 2,48,382 | ,, Yarn and Art. Silk Purchases ... | | 2,52,404 |
| 2,90 618 | ,, Bleaching and Dyeing Charges .. | | 2,44,329 |
| 1,45,571 | ,, Commission, Discount and Brokerage on Cloth, Yarn and Waste sales .. | | 1,84,372 |
| 2,55,289 | ,, Electric Power Supply ... | | 1,92,779 |
| 45,769 | ,, Coal and Liquid Fuel ... | | 48,005 |
| 16,12,320 | ,, Mill Salaries and Wages ... | | 16,08,003 |
| 14,925 | ,, Office Salaries ... | | 16,116 |
| 22,512 | ,, Office and Mill Establishment Charges Stationery and Printing | | 36,912 |
| | ,, Loss on Mill Grain Shop ... | | 34 |
| 62 890 | ,, Interest .. | | 83,237 |
| 30,156 | ,, Rates and Taxes ... | | 31,150 |
| 18,318 | ,, Fire Insurance .. | | 18,734 |
| 2,628 | ,, Workmen's Compensation Insurance Premium ... | | 2,793 |
| | ,, Government War Risks Insurance premium ... | | 4,216 |
| 7,900 | ,, Directors' Fees ... | | 7,000 |
| 1,000 | ,, Auditors' Fees ... | | 1,000 |
| 210 | ,, Law Charges ... | | 1,20,655 |
| | ,, Part Loss on Sale of Machinery | | |
| 18,000 | ,, Agents' Office Allowance and Salary .. | 18 000 | |
| | ,, ,, Minimum Commission | 40,000 | 58,000 |
| 4,013 | ,, ,, Commission Debited to Stores and Capital Accounts ... | 5,075 | |
| 48,53,053 | | 63,075 | |
| | | Rs. | 54,92,511 |

MILLS, LTD.
ended 31st December 1940

| 1939 Rs. | | Rs | Rs |
|---|---|---|---|
| | By Cloth Sold ... | 56 55,225 | |
| | *Less*—Opening Stock .. | 15,96,673 | |
| | | 40,59,552 | |
| | *Add*—Closing Stock .. | 11,85,454 | |
| 43,59,330 | | | 52,45,006 |
| | " Yarn Sold ... .. | 24,976 | |
| | *Add*—Closing stock ... | 73,662 | |
| | | 98,638 | |
| | *Less*—Opening stock ... | 81,783 | |
| 85,675 | | | 16,855 |
| | " Waste Sold ... ... | 1,80,918 | |
| | *Less*—Opening stock ... | 3,725 | |
| | | 1,77,193 | |
| | *Add*—Closing stock .. | 7,008 | |
| 1,60,987 | | | 1,84,201 |
| 10,525 | " Cloth Dyeing Charges ... | | — |
| 6 | " Transfer Fees ... ... | | 5 |
| 720 | " Sundry Receipts ... .. | | 720 |
| 2,85,810 | " Balance Being Loss for the Year (subject to Provision for Depreciation on the fixed assets) carried to Balance Sheet .. | | 45,724 |
| 48,53,053 | | | 54 92,511 |

## CHAPTER 5

### THE DIRECTORS' REPORT

Section 131-A requires that a directors' report dealing with the following matters shall be attached to every balance sheet :—

*(a)* The state of the company's affairs ; and

*(b)* The disposal of the company's profits, namely, (i) the amount which the directors recommend by way of dividend, and (ii) the amount which they propose to carry to reserves shown specifically on the balance sheet to which the report is attached or to be shown in a subsequent balance sheet.

The directors' report is to be signed by the same persons as are required to sign the balance sheet, but it may be signed by the chairman alone if he is so authorised by the directors.

The object of the report is to furnish additional information to the shareholders, and the requirements of the law may be explained as follows :—

*(a)* **The State of the Company's Affairs.**— Some directors' reports are very meagre—almost silent—on this point ; but in most cases they contain very useful information about the company's business e.g.

How the company has fared during the year under report and why ; prospects in the current year in which the report is prepared ; mention of any special difficulties such as coal shortage, labour scarcity, lack of stores and raw materials, increased cost of production, falling off in the demand for the company's products, birth of new competition, government interference, etc. ; out-put and sales ; expansion of business ; addition to block account ; changes in management, etc., etc.

The directors' reports of some companies are very elaborate indeed.

*(b)* **Recommendation as to Dividends** Interim dividends may be declared by the directors with their own authority if they are so authorised by the articles ; but the final dividends are recommended by them and confirmed by shareholders in ordinary general meetings. The shareholders cannot increase the amount of dividend recommended by the directors, but they can reduce it if they so like.

Where companies prepare half-yearly accounts and hold half-yearly ordinary meetings, there can be no interim dividends. Out of each half-year's profits a dividend is recommended by the directors and approved by the shareholders at the half-yearly general meeting.

The dividends proposed may be either without deduction of income-tax or subject to deduction of income-tax paid or payable by

the company ; and they may be declared either at so much per cent. or so much per share.

**Depreciation and Reserve Appropriations.** The directors have the power to make these appropriations before recommending a divi dend. Adequate depreciation they can always provide. In most cases *they also* have *the authority to make reserve appropriations without* the shareholders' approval; but in a few cases the reserve appropriations are also to be recommended by them for the shareholders' approval at the ordinary general meetiogs.

In the former case, the depreciation and reserve appropriations will appear in the balance sheet to which the directors' report is attach. ed ; while in the latter case they will appear in a subsequent balance sheet, i.e., the balance sheet prepared at the end of the year in which the ordinary general meeting is held.

The Iollowing extracts show how the reserve appropriations and the dividend recommendations appear in the directors' reports:

1. **The Bengal Paper Mills Co., Ltd.**

Director's Report for the Half-year ended 21st December 1940

| | Rs. | a. | p. |
|---|---|---|---|
| The profit for the half-year after providing for Debenture Interest, Depreciation and Taxation was | 3,58,393 | 5 | 11 |
| To which is added the balance brought forward of | 56,578 | 2 | 8 |
| *Total* | *4,14,971* | *8* | *7* |

Out of the total of Rs. 4,14,971-8-7 your Directors have set aside the following amounts :—

| | Rs | a. | p. |
|---|---|---|---|
| General Reserve | 54,845 | 7 | 7 |
| Raw Materials and Stores Reserve | 1,00,000 | - | - |
| Reserve for Indian Workers' Pensions and Gratuities | 10,000 | - | - |
| Total | 1,64,845 | 7 | 7 |

This leaves a balance of Rs. 250,126-1-0 available for distribution which your Directors recommend be dealt with as Iollows :—

| | Rs | a. | p. |
|---|---|---|---|
| Dividend on Cumulative Preference Shares at 7°/₀ p a free of Income-Tax | 7,000 | - | - |
| Dividend on "A" Cumulative Preference Shares at 7°/₀ p. a. free of Income-Tax | 14,000 | - | - |
| Dividend on Ordinary Shares at 25°/₀ p. a. free of Income-Tax | 1,12,500 | - | - |
| Bonus of Re. 1 per share on Ordinary *Shares free of Income-Tax* | *36,000* | - | - |
| Balance carried forward | 80,626 | 1 | - |
| Total | 2,50,126 | 1 | - |

**2. The British India Corporation, Ltd.**

Directors' Report for the year ended 31st December 1940

The profit for the year, after making all usual allowances including the sum of Rs. 7 lakhs for Depreciation, and including income from Investments, amounts to Rs 62,07,079–1–9 to which has to be added the amount brought forward from last year, namely, Rs. 1,86,778–1–11 making the total sum available Rs. 63,93,857–3–8. Your Directors recommend that this sum should be disposed of in the following manner :—

| | Rs. | a. | p. |
|---|---|---|---|
| 1. Transfer to Taxation Reserve | 42,00,000 | 0 | 0 |
| 2 Transfer to Rehabilitation Reserve | 3,00,000 | 0 | 0 |
| 3 Dividend for the year to 31. 12. 1940 on the Cumulative Preference Shares (8% p. a.) free of Income-Tax | 6,48,000 | 0 | 0 |
| 4. Dividend for the year to 31. 12. 1940 on the Ordinary Shares at four annas per share free of Income-Tax | 11,03,750 | 0 | 0 |
| 5. Carry forward to next Account | 1,42,107 | 3 | 8 |
| Rs. | 63,93,857 | 3 | 8 |

**3. The Muir Mills Co., Ltd.**

Directors' Report for the year ended 31st December 1940.

'After providing for a bonus to employees and setting aside Rs. 6,25,000 for estimated Taxation, Rs 2,50,000 for Depreciation and Rs. 20,000 to Pension and Gratuity Fund, the result of the year's working is a profit of Rs 4,98 741-8-4. Adding to this Rs. 1,26,154-3-5, being the balance brought forward from 1939, there is a sum of Rs 6,24,895 11-9 available which the Directors have allotted as follows :—

| | Rs. | a. | p |
|---|---|---|---|
| Ad Interim Dividend of Rs. 1-8-0 per share on the Preference Shares, Rs. 5 per share on the Ordinary Shares to 30th June (both free of Income-Tax) ... ... ... | 1,95,000 | 0 | 0 |
| Leaving for disposal a sum of Rs 4,29,895-11-9. which they propose to deal with as follows : | | | |
| Final Dividend of Rs. 1-8-0 per share on the Preference Shares (free of Income-Tax) ... | 45,000 | 0 | 0 |
| Final Dividend of Rs. 5 per share on the Ordinary Shares making 20°/o for the year (free of Income Tax) ... ... ... | 1,50,000 | 0 | 0 |
| Bonus of Rs. 2-8-0 per share on the Ordinary Shares (free of Income-Tax) ... ... | 75,000 | 0 | 0 |
| To be carried forward ... ... | 1,59,895 | 11 | 9 |
| Total Rs. | 6,24,895 | 11 | 9 |

### Management of Earnings.

The success or failure of a joint stock company depends in no small measure, upon the way in which its earnings are managed. This question needs very careful handling on the part of directors and managing agents; and it consists of two things, namely, computation of earnings and the distribution of earnings. How the profits of a company should be computed has already been discussed, and now the distribution of profits will be considered.

### Distribution of Profits.

Joint stock companies are run for the benefit of their shareholders. Therefore when the distribution of company profits is considered, the requirements of the shareholders should not be overlooked; for no management can last long unless it meets the wishes of the controlling group. What are the interests of the shareholders and how do they clash with the short term and long-term functioning of the company?

The *shareholders of many large companies cannot be regarded* as a permanent body of individuals, as the shares constantly change hands in the stock market. Many shareholders do not regard their holdings as permanent investments, but rather as temporary investment which they may sell at any opportune moment or at any time when they need money. Naturally such shareholders desire to secure as large returns as possible and do not desire to have earnings withheld in order that future shareholders may reap the benefit. *Their first interest is not in the company but in themselves.* Actually there are many companies in which the interest of the shareholders and the interest of the company are not identical. In such circumstances, which interest should the directors serve? Pixley in his book "Auditors: Their Duties and Responsibilities" expresses his opinion as follows:

'It is not incumbent upon the directors to consider in any way individual shareholders or a special group of shareholders, and certainly not those who make a practice of buying and selling shares and holding them for short periods. It is their duty to keep the capital of their company intact, and to do their best to make a permanent institution."

Practically the same observations were made by Mr. (now Sir, Robert Menzies, Chairman of the British India Corporation Ltd., Cawnpore, at its annual general meeting held on 27th March 1943, when he said:

"Your Directors, in recommending that the dividend on the ordinary shares should be maintained at 25 per cent., have had before them the fact that the period of recovery after the war should, as I have stated before, be difficult and costly and, further that it was their clear duty to safeguard, to the fullest extent possible, the interests of, what I might call, the *bona fide* shareholders of The Corporation. I do not regard it is the Directors' duty to the same extent to safeguard the interests of speculators who may be induced to buy or to sell share in public companies in circumstances involving a risk of loss or a possibility of gain. Speculators are prepared to take a chance and presumably are also prepared to pay for it, if necessary."

Equally forceful and dogmatic opinions are often expressed by shareholders on the otherside Perhaps the most practical conclusion

that can be reached is that the directors shnuld consult both sets of interests ( i. e., the interest of the company and that of its shareholders ), and when necessary should compromise. They should certainly protect and keep intact the property nf the company, hnt at the same time they should endeavour to avoid injnrinus concealment of facts or injustice to the present shareholders as compared with the snceeding ones.

The law ( regulation 95 of the Table A which is compnlsory for all companies ) provides that the declaration of dividends is nptional with the directors ; and the articles nf almost all companies contain a provision similar to regulation 99 nf Table A which provides that, before declaring a dividend, the directnrs have power to make such reserves as they may think proper. And in the case of hanking companies, section 277-K of the Indian Companies Act makes the creation of a reserve fund compulsory before any dividends are declared.

Thus the directors of companies are empowered to determine the amount of current income to be set aside for working capital and the amonnts of dividends to he distributed to shareholders. In recent years, however, the power of directors in this respect has been to a large extent restricted hy the Government's taxation measures.

Until the directors recommend a dividend, there is no way in which the shareholders can control their action. The directors are the trustees for the shareholders, and they are given power to dispose of the funds of the company. Nn matter how large the profits of the company, there is no way in which the directors can he compelled to declare a dividend. The shareholders can only participate in profits through the channels provided hy law. They can invoke the aid of the courts to prevent the diversion of the company's funds to nnlawful objects; they can restrain the directors and nfficers from paying to themselves exorbitant salaries; and they can prevent any improper nse of the company's profits. But, as long as the directors leave the company's profits with the company and until they decide that a dividend should he paid, the shareholders cannot obtain any share of these profits. Their only power, in case they are dissatisfied with the management of the company, is to elect new directors or sell off their shares and withdraw from the company

Unless the memorandnm or the articles of association of a company make a clear provision that the whole of the company's profits shall be divided among the shareholders, the company is not bound to do so. Whether the whole or a portion or what portion shall be divided among the shareholders are questions nf internal management of a company and the courts have no jurisdiction to interfere. These are questions for the shareholders to decide subject to any restrictions or directions contained in the articles nf association of the company.

### Correct Financial Policy.

When the profits of a company have been correctly determined, tbey are not all available for distribution to shareholders. What are, then, the essentials of a correct financial policy to be pursued by the directors of a company in regard to the distribution of its profits ? These essentials may be put down as—

1. The legal aspect of the qnestion;

2. Cantion, i.e., the proper conservation of the company's resonrces ;
3. Moderation and consistency, i e , the proper relation between the company's profits and its dividends ; and
4. The ways and means positinn of the company.

Each of these four essentials will nnw be examined io detail.

1. **Legal Aspect** — When considering the disposal of a company's profits, the directors should carefnlly examine the legal aspect of the question. The net profits ( or actual or trne profits ) of a business are said to be the surplus of current incnme for a given period over current expenditnre for that period after making good any losses on floating assets and after providing for the expired capital nriginally snnk in fixed assets. But the term 'divisible profits' means all profits that can be legally distributed to the shareholders nf a company in the shape of dividends. According to regulation 97 of Table A, which applies to all companies, no dividends can be paid otherwise than out of profits of the year or any other undistributed profits. The profits may consist of profits arising from trading and those arising from other sources. It is not the law that dividends can be paid only ont of trading profits.

The company law does not lay dnwn the manner in which the profits of a company are to be ascertained nor does it define what profits can be used for dividend purposes. The law has abstained from formulating rnles for the guidance and embarrassment of business men in the conduct of their business affairs. These matters are left entirely to the memorandum and articles of the company. There are, however, two principles which must be applied in determining, in any given case, whether a particular profit is available for dividend or not viz.—*(i)* That in no circnmstances is a dividend paid out of capital ; and *(ii)* That in every case the requirements of the company's memorandum and articles are faithfully complied with.

In the absence of adequate statntory provisions on the subject of divisible profits, difficulties have from time to time arisen in practice with regard this question, and there are a nnmber of important cases bearing on the subject decided by the courts. The difficulty that has arisen in the disputed cases is the true meaning of the term 'profits', i. e., what can be legitimately included in profits available for dividends and what losses must be made gond nnt of those prnfits before they can be distributed. It is, however, certain that the legal definition of profits is much wider than its commercial meaning as explained above.

Therefore the difficult qnestion nf what are profits available for dividend in a particular case can be decided only ater a careful consideration of the following legal decisions:—

*(i)* **Depreciation of Fixed and Floating Assets.** Although as a matter of prudent business policy the depreciation of fixed assets such as buildings, plant and macbinery, etc., which are gradually worn out in the process of earning profits, must be made good, and similarly losses of floating assets must be replaced, yet the legal aspect of the subject of depreciation of fixed and floating assets as affecting limited companies is somewhat different, viz.—

*(a)* The depreciation of floating assets must be made good before the paymeot of a dividend, because if the income of any year arises from a consumption in that year of floating assets, the division of such iocome as dividend without replacing the capital consumed in produciog it will be a payment of dividend out of capital. Verner v. General aod Commercial Investment Trust, Ltd.. 1894.

*(b)* According to the decisions in Lee v. Nauchatel Asphalte Co. Ltd. , 1889, Verner v. General and Commercial Investment Trust, Ltd., 1894, and other cases, it appears that a company is under no legal obligation to make good depreciation of its fixed assets, provided there is nothing io its articles requiring it to do so and that it retaios sufficient assets to discharge its liabilities.

*(c)* Where it is proposed to pay a dividend out of realised capital profits, the depreciation of both fixed and floating assets must be made good. Lubbock v. Britisb Bank of Soutb America, 1892 aod Foster v. New Trinidad Lake Asphalte Co., Ltd., 1901.

*(ii)* **Past Losses.** Sometimes a loss in one year is followed by a profit in the next. In the interest of sound company finance only the excess of profits over previous losses should be distributed; but that is not the view taken by the law. It was held in Ammonia Soda Co. v. Chamberlain, 1918, that the directors of a company may, in the honest exercise of their discretion and subject to the articles of the company, divide a profit arising in a period of account, even though losses of previous periods remain unabsorbed.

The Hukumchand Jute Mills, Ltd. had on 31st March, 1943 a debt balance of Rs 6, 05, 872-14-6 in its profit and loss account, and in the following half-year it made a profit of Rs. 7, 78, 220-10 2, out of which it reserved Rs. 4, 50,000 for taxation and distributed Rs. 2, 80 000 by way of preference share dividend, leaving only Rs 48, 220-10 2 to be adjusted against the past accumulated loss. That is to say, it distributed as dividend the profits for the half-year ended 30th September 1943 without making good past losses.

Whether a company making profits and losses io alternate years could treat each year's profit and loss account separately, dividing the profits in years when profits were earned, whilst iogoring the losses in years when losses were incurred, has not yet been legally decided Possibly such a course if persisted in, would be held to be evideoce of the absence of an honest exercise of the directors' discretion, and would not therefore be permitted.

*(iii)* **Capital Profits.** As stated above it is not the law that divideods can be paid only out of trading profits. Non revenue profits may also be used for dividend purposes in the following circumstaoces :—

*(a)* Capital profits are available for the payment of cash divideods ooly *(i)* if their distribution is not repugnant to the company's articles ; *(ii)* if they actually realised in cash *(iii)* if they remain after a revaluation of all the assets and liabilities of the company ; and *(iv)* if their distribution would not leave the company insolvent io the sense that it is unable to pay its debts as and when they fall due for payment. Lubbock v. British Bank of South America, 1892 ; Foster v. New Trioidad Lake Asphalte Co. Ltd., 1901.

*(b)* The question as to whether an unrealised capital appreciation in the valne of a fixed asset can be distributed in cash does not appear to have been legally divided; but it wonld certainly be inadvisable and in most cases improper to write np the value of fixed assets with a view to declaring a dividend, even if sucb assets had really increased in value, because such a profit is not realised aod may never be realised. But capital profits arising on a bona-fide revaluation of fixed assets can be ntilised to write off a debit balance on the Profit and Loss Account arisiog in previons years, thus enabling dividends to be paid out of current profits. Ammonia Soda *Co. V. Chamberlain*, 1918.

*(c)* Capital profits, whether realised or not, can always be utilised for distribution in the form of bonos shares, since the assets are not thereby reduced in any way.

*(iv)* **Draft upon Reserves-Open or Secret.** Regulation 97 of Table A which is compulsory for all companies, permits the distribution of dividends out of past ondistribnted profits. Profits available for dividends, if carried to reserve, do not cease to be profits unless and nntil tbey are effectually capitalised e. g., by the issue of bonus shares. A reserve formed out of profits retains its character of profits and is capable of future division as such. But profits ooce capitalised cannot afterwards be decapitalised in order to make them available for distribntion as dividend.

Where a company holds secret reserves created by over depreciating its fixed assets, snch secret reserves may be utilised for dividend porposes. The fixed assets over depreciated in the past may be written np by the amonnt of socb over depreciation and the amonnt thns rendered available may be ntilised for dividends provided (*i*) the procednre is not contrary to the company's memorandom or articles; and (*ii*) the value to which the fixed assets are written np is not in excess of their true valoe. *Stapley v.* Read Bros, Ltd., 1924.

If a loss has been sostained in a particular year, bot there is an accumnlation of past profits, the latter must first be applied against the loss, and only the balance if any, is available for dividends.

If a company reduces its share capital under section 55 of the Indian Companies Act, and it holds at tbat time aoy general reserve, such reserve cannot thereafter be ntilised for the payment or equalisation of dividends.

(*v*) **Transfers to Reserves** If, as is osnal, the directors of a company are empowered by the articles to set aside reserves out of profits before ascertaining the amoant available for dividends, their discretion cannot be questioned, and the profits available for dividends are the profits remaining after such reserves have been set aside. Bond v Barrow Hoematite Steel Co., Ltd , 1902.

*Note.*—From what has been stated above, it is obvious that in the matter of divisible profits the legal view is mnch wider than the strict commercial meaning which aims at making good all losses whether capital or revenue before the ascertainment of profits. In practice, however, companies, as a general rule, ascertain their profits on sound business principles, and do not distribute in dividends the whole of the profits which they may be legally entitled to treat as such, without making at least reasonable provisions for meeting losses on capital.

2. **Conservation of Resources.** The interests of a company demand that its capital shall be kept intact and that its resources shall be consolidated and strengthened. Before ascertaining the amount that can be properly used for dividend purposes, the directors must, therefore, make certain *essential* and *desirable* provisions—essential provisions in respect of depreciation and taxation and desirable provisions in respect of transfers to various reserves

*(a)* **Depreciation.** In considering the earning capacity of a company, one of the principal factors to be taken into account is the extent of the provision that has been made in the past or has to be made in the future for depreciation. Depreciation has been defined as the shrinkage in value caused by the wearing out of an asset owing to its use in the business, and the provision for it represents the allowance made in the balance sheet for such wear and tear.

Depreciation in the value of fixed assets may be due to wear and tear, obsolescence, etc. Depreciation on account of wear and tear may be estimated in advance with some accuracy, but depreciation for obsolescence is always of uncertain amount. No one can foresee what changes in taste or fashion, what unthought of inventions, or what improvements in organisation may take place, which will perhaps render useless or partly useless much of the company's plant, machinery or other assets The best that can be done is to make a fairly liberal estimate, based on the experience of the past and trust that it will be sufficient to keep the book value of fixed assets always well within the limits of actual value. If this result is not accomplished, then the depreciation provision is inadequate and the figure of profit is overstated.

"Before finally settling the amount of profit available for distribution, the question of depreciation has to be carefully considered. This is a most important matter for which the directors are completely responsible The fixed assets gradually lose their value, more or less according to the manner in which they are used; and for this reason no company can be said to have made a fair profit until, in addition to the expenses of its business, there has been charged against the revenue a proper amount for depreciation in respect of its fixed assets." Withers: *Stocks and Shares.*

It is obvious, therefore, that a proper provision for depreciation must be made in the profit and loss account before arriving at the amount of true profits. Depreciation should be regarded in the nature of working expenses. In practice depreciation is looked upon by company managements in some cases as working expenses, but there are many instances where depreciation is not deducted for ascertaining profits, although it must be before giving a dividend. It means that in the majority of cases provision for depreciation is made only when there are profits, and it is not regarded in the nature of a working expense. If there are no profits, depreciation is not provided for, but the arrears of depreciation are carried forward to be made good in future when there may be profits. On the other hand in the case of companies under the management of managing agents, who follow a prudent and conservative financial policy, provision for depreciation is always made before arriving at the figure of profit or loss.

The fact that provision for depreciation is not regarded as a working expense but merely a transfer from profits is supported by

the following extracts taken from chairmen's speeches at company meetings :—

"The directors feel it their duty to conserve profits in the building up of reserves and the elimination of assets, the full value of which is problematical." (Spencer & Co., Ltd.)

"Speaking last year on a similar occassion, I expressed the hope that within a further period of three or four years we will have entirely recouped the block account from our working profits and our entire capital would be held in liquid and floating assets. Under the policy pursued by your directors we have every reason to feel that this position may be realised earlier than anticipated." (The Mysore Chemical and Fertilisers, Ltd.)

It is this conception of depreciation that leads to arrears of depreciation. If the orthodox method is followed, viz., if depreciation is provided for whether there are profits or not, there can be no question of arrears of depreciation. In the case of some of the cotton mill companies, depreciation is on the recommendation of directors finally sanctioned by the shareholders in general meetings, e. g., The Simplex Mills Co., Ltd., The Vijaya Mills Co., Ltd., The Ajit Mill, Ltd., and The Pankaj Mills, Ltd. But this is rather an unusual procedure.

**Legal view of depreciation.** Although, in addition to expenditure on renewals and repairs of fixed assets, all well-conducted concerns make provision for depreciation whenever they earn profits, yet there is no statutory obligation to do so, unless the memorandum or articles of the company so provide. Regulation 107 of Table A, which prescribes the contents of the profit and loss account, does not mention that depreciation should always be provided for, because it merely states that every item of expenditure fairly chargeable against a year's income shall be brought into account. A specific reference to depreciation in the Indian Companies Act is contained in the provision prescribing the basis of the remuneration payable to managing agents in agreements entered into after 15th January 1937. In sub-section (3) of section 87C, the net profits on which the remuneration is to be assessed are defined as profits calculated after allowing the usual working charges and depreciation. The basis for providing for this depreciation is, however, not prescribed and it is with the directors of a company that discretion rests in the matter of determining the depreciation to be provided for.

**How depreciation is assessed.** The exact method of assessing the amount of depreciation to be provided for depends largely upon the financial policy pursued by the management of a company. Where a conservative and cautious policy is adopted more than the necessary amount of depreciation is charged in the accounts. The entire loss caused by the Bihar earthquake in 1934 was charged to the profit and loss accounts of one year only in the case of Begg Sutherland's sugar mills. During the half year ended 30th June 1943, the Bengal Flour Mills Co., Ltd., sold some superfluous plant, and out of the excess of Rs. 1,11,139 realised from the sale Rs. 42,197 was used to write down buildings and the remaining plant, machinery and furniture to Re. 1 each. There are many instances of such over depreciation in the Eastern Presidency where the European managing agents have followed consistently a policy of cautious finance in the matter of providing depreciation. By following this policy of generous depreciation colossal

secret reserves exist in many companies. While reviewing the accounts of a Bengal company, "Watchdog" wrote as follows in the Investor's Supplement of *Indian Finance* dated 4th May 1935 :

"The policy of depreciation has been carried out so zealously that I am constrained to reiterate my criticism against the policy. There is every reason for calling a halt to this non-stop depreciation. The term "equity" will be rendered a misnomer, if pharisaic finance were to deprive the holder thereof over an indefinite period of the fruits of cautious abstinance in the past."

Quite a large number of companies are now adopting the method of providing for depreciation on the 'scale down' basis at the rates allowed for income tax purposes, if the profits permit such a course. Prudent managing agents, however, make provision for special depreciation as well in addition to the normal allotment at the statutory income-tax rates, e. g. :—

"The Directors are strongly of the opinion that the statutory allowance of one and a half times the single shift rates is insufficient to cover double shift working, particularly under war-time conditions and therefore in addition to depreciation in accordance with the statutory Income-tax rates amounting to Rs 5,41,117 they have set aside a further sum of Rs. 2,50,000." Directors' Report of The Kohinoor Mills, Ltd., Bombay, for the year ended 31st December 1943.

The practice of writing off depreciation irregularly by arbitrarily setting aside such sums as can conveniently be spared out of the annual profits is one that cannot be recommended. This practice is followed, it is true, by some of our well-managed concerns. But it is essentially unsound. Depreciation is not a theory or a vague notion in some one's head ; it is an actual element in the operation of every business ; it is going on day and night, through all seasons ; year after year ; in periods of depression as well as in periods of prosperity. The losses due to depreciation should constitute, therefore, a regular charge against gross income. The amount of that charge should be estimated as accurately as possible and should be adhered to year after year ; otherwise we get a purely fictitious showing of net profits. If large sums are charged off in one year and nothing is charged off the next year, the final showing of profits in the two years may be about uniform, whereas the business has perhaps really suffered an enormous fluctuation. The purpose of accounting should be not to conceal such facts, but faithfully and clearly to set them forth. Lough : *Business Finance.*

On the other hand, the necessity of adhering to a rigid standard in making actual provision for depreciation is also sometimes questioned in view of the fact that, as experience in England and in India shows, the life of a plant is not necessarily limited to what it is calculated. Moreover it has to be recognised that to allow for depreciation at a statutory rates in concerns which are overcapitalised imposes a needless burden and leads to an incorrect position being presented of the profit-earning capacity of the industry or of a particular unit. Bombay Textile Labour Inquiry Committee Report 1940.

**Amount of depreciation.** In making provision for depreciation and in judging its adequacy, the following factors should be considered :

**1. The extent of the profits.** Where depreciation is charged before ascertaining the profit or loss, this question does not arise. Depre-

ciation does not depend upon the amount of profits. But in cases in which depreciation is provided for only when there are profits, the size of the profits is an important factor, which cannot be overlooked.

2. **The need for some dividend.** Sometimes it is expedient for the management of a company to allow small dividends even if full provision for depreciation cannot be made. One reason for this may be the maintenance of the market value of the company's shares. The Kesoram Cotton Mills, Ltd., is an example of a company, which has declared dividends without making adequate provision for depreciation. *The Commerce* dated 16th October 1943, while reviewing the accounts of this company for the half-year ended 31st March 1943, criticised this policy as follows:

"In spite of providing Rs. 1,889 lakhs for depreciation during the last two years ended 31st March 1943, there seem to be still some arrears on this account. It is to be hoped that, before the present favourable conditions for the Indian cotton mill industry fade out, the management will be able completely to wipe off all the arrears and to provide substantial sums for replacements and renewals in the post-war period. This it should endeavour to do even by reducing the dividend level, if necessary; for we believe that there is no point in paying high dividends without first clearing off all arrears of depreciation."

3. ***Condition of the assets.*** The amount of depreciation to be provided for must depend upon the condition of the assets. If the assets are new there is much less need for depreciation or if the assets are kept in proper repair the need for depreciation will be less.

4 ***Past excessive depreciation.*** If too much depreciation has already been written off in the past, the need for its future provision will be less e g,

"For many years it has not been customary to charge depreciation in the accounts of this Company as it was considered that owing to excessive depreciation having been set aside in the past the assets had already been sufficiently written down But the advent of modern jute spinning machinery has shown that most of the machinery and buildings now owned by the company are likely to become obsolete before many years are past. Your directors have, therefore, decided to charge depreciation at approximately the rates recently proposed by the Board of Revenue ( Income-Tax )." Directors' Report of The Clive Mills Co., *Ltd., for the half-year ended 31st March 1940.*

5. **Consideration for past arrears.** In settling the amount of depreciation to be provided for, the past arrears, if any, should be taken into account. The Apollo Mills, Ltd., Bombay, provided for depreciation Rs. 10 lakhs in each of 1941 and 1942 but only Rs 5 lakhs in 1943, because in the first two years the depreciation provision included the arrears accumulated in the depression years preceding the outbreak of war.

6 **Size of other reserves.** If a company holds ample reserves apart from depreciation, these can easily support the block account, and a cut in the depreciation amount need not be considered serious. if that has been necessitated by reduced earnings. In reviewing the accounts of Indian Steel and Wire Products, Ltd., *The Commerce* dated 27th October 1943 wrote in this connection as follows :-

"Although the reduction in the earnings has necessitated a cnt in the provision for depreciatinn, snch need not be viewed by the shareholders with concern in view nf the Company's strong financial position. Its fixed assets have already been adequately depreciated aod its reserves are substantial and are well represented by liquid assets"

Again, *The Commerce* dated 15th January 1944, while reviewing the accouots of Indian Iron and Steel Co, Ltd, stated :

"Despite the fall in profits, the directors have maintained the allocation to depreciatioo at Rs. 25 lakhs. Io fact, this provision would have been higher, as was indicated by Mr. Martin in his address to the shareholders at the last year's annual general meeting. The Board, however, decided not to do so in view of the iocrease in the provisioo for repairs and renewals from Rs 6,78 lakhs to Rs. 10 79 lakhs."

7. **Amount written off on reduction nf capital nr revaluation of assets.** If on the reconstruction of the capital structure of a company or on the revaluation of its assets, ample amounts are written off the block account, the need for future depreciation is correspondingly redneed. The effect of the revalution of assets is to change the base on which depreciation charges are computed, if depreciation is to be calculated at the statutory rates prescribed for Income-tax purposes.

The Indian Iron and Steel Co., Ltd., provided for the year ended 31st March 1942 a sum of Rs. 25 lakhs for depreciation as against only Rs. 14.80 lakhs in the previous year and the Chairman of the Company explained this difference as follows :—"On the amalgamation of your Company with the Bengal Iron Company some five years ago, it was decided that, having regard to the reduction of capital which was made at that time, depreciation for the subsequent few years should be taken on a lower basis than would otherwise have been necessary. The time has now come when the annual figure of depreciation must be taken on a more normal basis and this explains the difference between the two above stated figures. It may be that next year we may have to still further enhance the sum set aside on this account."

**Depreciation in war-time,**—During the recent war-boom period, it has been necessary for industrial companies to make greater provision for depreciation on account of the following reasons :—

1. In order to consolidate the financial position with a view to meeting the post-war difficulties, wheo there may be fierce competition to be faced aod when plant and machinery may have to be replaced.

2. Most of the companies are enjoying war time prosperity in the form of greater profits aod it is possible to make a correspondingly greater provision for depreciation.

3 Plant aod machinery in almost all industries are being subjected to the maximum strain possible by double and multiple shift working and consequently there is greater wear and tear.

4. Some companies have had to purchase special equipment to cope with war orders. Now that the war is over and war orders have ceased, this special plant will become useless and will have to be discarded entirely. It is therefore necessary that this special plant should be completely eliminated out of war profits, if possible.

5. In many cases, proper repairs of assets have been neglected partly because the mills have been too busy to stop work for repairs and partly because enough spare parts have not been easily available.

6. Capital assets acquired during the war have been purchased at inflated prices, and must therefore be adequately depreciated.

7. Depreciation is all the more necessary in a boom period because there is the practical certainty that the boom will decline more or less suddenly and will leave the assets overvalued.

8. The replacement costs are and would remain for some years' to come much higher than in normal times.

*(b)* **Taxation.** Since the outbreak of the last war, taxation on company profits has been progressively increased—from 24 pies in the rupee to 57 pies and even to 69 pies on those profits that are distributed as dividend on ordinary and deferred shares. Then there is the excess profits tax, gradually increased from 33-1/3 to 66 2/3 per cent of the excess profits over the standard profits The actual incidence of E.P.T. depends upon the standard profits. If the standard year is favourable, the E.P.T. burden is comparatively light; but where the standard year is unfavourable as in the case of most Bombay cotton mills or where the companies have no standard period because they were started after the outbreak of war, the E.P.T. is a heavy impost. The profits of the standard year are also favourably affected by an increase in the capital employed brought about by retention of profits in the business and also by an increase of the share capital.

Section 10 (1) of the Indian Finance Act of 1942 provided that companies could make an optional deposit of 20% of the E.P.T. paid with Government and would get 2% per annum interest thereon. This can be withdrawn within twelve months of the end of the war or two years from the payment of the deposit whichever is later. The Government would also refund 10% of the E.P.T. paid as bonus which would be released in accordance with rules which were framed in consultation with the Reconstruction Committee of the Government of India. The purpose of these rules is that Government's contribution will be released within three years of the end of the war or earlier if the assessee is able to establish a claim for advantageous use of the money at an earlier stage. This provision was intended to serve as an anti-inflationary measure and as an indirect limitation of company dividends.

In May 1943, however, this optional deposit was converted into a compulsory one by section 2, (1) of the E.P.T. Ordinance No XVI of 1943 with the intention of serving it as an anti-inflationary measure and indirect limitation of dividends. This compulsory deposit was to be made in respect of any C.A.P. ending after 31st December 1942.

By the Indian Finance Act of 1944 the compulsory deposit has been raised from 1/5 of E. P. T. to 19/64 of E. P. T.; while the Government's contribution remains the same, namely, 1/10 of E. P. T. paid. This compulsory deposit is now to be made as soon as the provisional assessment has been completed. This provision is to apply to any C. A. P. ending after 31st December 1943. The effect of this provision will be to immobilise as deposits the whole of the excess

profits remaining after E. P. T. has been paid on them and income-tax and snpper-tax bas been paid on the balance.

The present incidence of taxation on companies may be illustrated as follows: For every rupee of excess profits, Re. 0-10-8 will go towards tbe E. P. T and Re. 0-2-2 towards income and corporation tax (the latter at 2 annas in the rupee). The balance left is Re. 0-3-2 (or 19/64 of Re. 0-10-8) which is tn be compulsorily deposited with the Government in respect of any C A. P. ending after 31st December 1943. The resnlt then is that, in every case, the amonnt available will be the standard profits minns income-tax and corporation tax on them at current rates. It follows, therefore, that few concerns, if any, can maintain their pre-war scale of dividends, and, as if that is not enough, the Government will charge an extra anna as corporation tax on dividends paid on ordinary and deferred shares. In other words, the Government first sees to it that few concerns can pay the pre war level of dividends and then it fnrther sees to it that, in the rare exceptions where snch dividends could be maintained, it is not worth the while of snch concerns to maintain such dividends.

The foregoing conclnsion is based on a careful analysis of the provisions of tbe Indian Finance Acts of 1944 and 1945. On a purely theoretical hasis the conclusions seem snbstantially to be correct. But when applied to the profits of individnal companies, the resnlt may differ from the above conclusions. For it should he remembered that the standard profit will he not only the profit earned in the standard year but will also include the percentages allowed by the authorities for the Increase in the working capital over the standard year. This point bas been well brought out in the following passage :—

"It should be noted that for the purpose of calculation of excess profits, the bare profits of the standard years are not the only consideration, but the accumnlated reserves for the last few years and the increase in share capital of compânies are also given due weight in the assessment of standard profits, and hence the base of standard profit is being raised every year."

**Prnvision for Taxation.** In pre-war times the Incidence of taxation on companies was comparatively light, as the rates of income-tax and corporation tax were reasonable and there was no excess profits tax. It was therefore not always considered necessary to make a separate provision for taxation before declaring dividends. Taxation was charged to profit and lnss acconnt as and when it was actnally paid.

Since the outbreak of the last war in September 1939, taxation on companies has, however, assnmed a special importance in connection with the management of their earnings, because its incidence has steadily increased. After setting aside an adequate amount for the depreciation of block, the first claim on the remaining profits of the company is that of Gnvernment. On this point Sir Robert Menzies, Chairman of tbe British India Corporation, Ltd., Cawnpore, made the following apt remarks at its annnal general meeting held in March 1944 :—

"In days gone by, the control of finance in a Corporation such as yours, was a matter meriting the cnnstant attention of the Directors, but, in the circnmstances which war has brought in its train, the

financial control of manufacturing concerns is gradually being assumed with greater and greater force by the Hon'ble Member for Finance in India. The Finance Member was a few years ago regarded, on the introduction of the excess profits tax, as the senior, but sleeping, partner of most business concerns in India and, as time goes on, he certainly continues to increase his interest in the disposal of any profits earned as the result of industrial or commercial enterprise; in fact his share of the profits now has attained such dimensions that there is little incentive left to increase either efficiency or production."

Therefore sound finance requires that, before fixing the amount of dividends payable to shareholders, a company's taxation liability in respect of income tax. corporation tax and excess profits tax based on the year's profits should be carefully estimated, if necessary in consultation with its auditors, and an adequate reserve set up therefor. This is the method followed by all well-managed concerns in India. Companies which prepare their accounts half-yearly provide for taxation in each half-year's accounts. The taxation reserve is created by the directors and appears in the published balance sheet and profit and loss account as well as in the Directors' Report.

If on the completion of the company's assessment the taxation reserve in existence is found to be excessive, the excess is dealt with in two ways. It is either credited back to profit and loss account, or else it is taken into account when making provision for the next assessment. Both these methods are illustrated by the following extracts from Directors' Reports :—

"The audited profit and loss account for the half-year ended 30th September 1943, after allowing for taxation including excess profits tax, etc. and transferring Rs. 4,50,000 from Taxation Reserve, which it is considered is no longer required on account of tax liability for previous accounting periods, shows a balance of Rs. 26,40,679-12-5." The Titaghur Paper Mills Co., Ltd.

"An appeal made by the Company to the Central Board of Revenue in connection with Excess Profits Tax has been upheld As a result, a sum of approximately Rs. 68,400 is due to be refunded, and this sum has been taken into account in the amount now reserved for taxation, which it is considered is sufficient to meet all taxation liabilities at current rates up to the date of closing." The Cawnpore Textiles, Ltd.—Half-year ended 31st March 1943.

Almost all companies liable to taxation set up a special reserve for it; but there are still a few companies which do not do so on the ground that they cannot estimate their taxation liability. Such companies, however, carry forward a sufficiently larger amount of profit with a view to meet the taxation liability when it is actually settled by authorities. The Directors of the Kesoram Cotton Mills, Ltd., in their Report for the half-year ended 30th September 1942 stated in this connection as follows :—

"The Directors have not made any separate provision for the taxation because the Company's E. P. T. case has not been finally decided. They think, however, that the amount shown in the carry-forward is more than adequate."

**E. P. T. Deposits.** Since May 1943 companies liable to E. P. T. have been required to make a compulsory deposit with Government. the amount of such deposits being based on the amount of E. P. T. paid. An interesting point about the compulsory deposits is that they are neither a tax nor an expense, and they are not in themselves debitable to profit and loss account. They are purely an investment. It may therefore be asked : How can the deposits affect dividends ?

The answer is that the deposits, although an investment, are a blocked asset which cannot be freed until after the war, and the company is therefore deprived of liquid finance to that extent and unless it is prepared to see a cumulative deterioration in its liquid resources, it must counteract these outgoings by conserving a portion of the profits inside the business. In other words, it must limit or reduce dividends.

The manner in which the matter have been dealt with in the accounts of companies varies with individual circumstances, but it is clearly undesirable that the amount carried forward on profit and loss account should be allowed to grow continually larger as a result of these necessary conservations. In practice the matter of compulsory E. P. T. deposits has been treated as follows :—

1. A separate reserve for E P. T. deposits is created in addition to taxation and other reserves. This is, of course, the best way of dealing with the matter, but it is possible only when a company's profits are sufficiently large.

2. A separate reserve for E. P. T. deposits is created in addition to the taxation reserve, but transfers to other reserves are omitted in order to compensate for the E. P. T. deposit reserve.

The directors of the Century Spinning and Manufacturing Co., Ltd., out of its profits for the year ended 31st December 1943, created a Taxation reserve of Rs. 1,37,00,000 and an E. P. T. Deposit Reserve of Rs 21,24,000, but omitted to make any transfers to either the Reserve Fund or the Dividend Equalisation Fund to which decent sums had been allocated in previous years.

The directors of the Ganges Manufacturing Co., Ltd., out of its profits for the half-year ended 30th September 1943, created a Taxation reserve of Rs. 8,64,075 and an E. P T. Deposit Reserve of Rs 1,36,000, but did not make any transfer to Contingency Account, as they considered that the amount reserved for E. P. T. deposit suitably covered the amount which would have ordinarily been reserved for Contingency Account.

3. No separate reserve for E. P T. deposits is set up, but the amount of E. P. T deposit is included in Taxation Reserve, and transfers to other reserves are maintained.

The directors of The Delhi Cloth and General Mills Co , Ltd., out of its profits for the year ended 30th June 1943, reserved Rs 1. 70 crores for taxes and E P. T. deposits, and they also transferred Rs. 1 lakh to Charity Reserve Rs 15 lakhs to Reserve for Fall in Prices, Rs. 10 lakhs to Reserve for Dividend Equalisation and Rs. 6 lakhs to General Reserve.

4. No separate reserve for E. P. T. deposits is set up, but the amount of E. P. T. deposit is included in Taxation Reserve, but transfers to other reserves are dropped.

The directors of the Bombay Dyeing and Manufacturing Co., Ltd., out of its profits for the year ended 31st December 1943, created a reserve of Rs. 2·79 crores for taxation which included not only the actual taxation payable but also the E. P. T. compulsory deposit, but nothing was transferred to Reserve Fund or Dividend Equalisation Fund, to which decent sums had been allocated in previous years.

5. The E. P. T. deposit is not separately provided for nor is it included in taxation reserve, but it is covered by transfers to other reserves which will not be utilised until the deposit matures.

The directors of the Pankaja Mills Ltd., out of its profits for the year ended 31st December, 1943, reserved Rs. 25·2 lakhs for taxation which did not include provision for E. P. T. deposit, and transferred Rs. 4. 75 lakhs to Reserve Fund which was intended to cover the E. P. T. deposit.

Similarly the amount of E. P. T. deposits was transferred in the case of Muir Mills Co., Ltd., to Deferred Mill Renovation Reserve; in the case of Buckingham and Carnatic Co, Ltd., to Reconstruction Reserve; in the case of the Gold Mohur Mills, Ltd, to Reserve Fund.

6. No provision is made for the E. P. T. deposits in any of the above ways; but a sufficient amount is left to be carried forward for this purpose.

The directors of the Phoenix Mills, Ltd., out of its profits for the year ended 31st December 1943, made no provision at all either for taxes or for the E. P. T. deposits, but decided to carry forward to the next years's account a som of Rs. 52,81,908, which was subject to income, corporation and excess profits taxes and compulsory E. P. T. deposit.

If a company goes on paying the E. P. T. compulsory deposits without in any way retaining an equivalent amount of profits, its liquid position is bound to deteriorate.

An incidental question that may be asked is whether the Government's contribution which will be payable after the war may be taken into account at once. The answer is obviously no, because it would be bad finance to discount the future when things are so uncertain. In fact, no company has taken credit for this contribution in its accounts, and this point is sometimes stated in the Directors' Reports or the profit and loss accounts.

**Information re E. P. T. to shareholders.** In view of the high taxation to which the companies are now subject, it is essential for the shareholders to know the facts, so that they may be able to assess the dividend prospects with some degree of accuracy. It may be mentioned that it has now become the accepted practice among all the leading joint stock companies specifically to indicate the E. P. T. compulsory deposits, so that the shareholders may have an idea as to whether or not the sums earmarked for reserve funds will be sufficient to meet such deposits *The Commerce* dated 25 March 1944.

Ever since the introduction of the provisions to immobilise the entire excess profits, the inquisitiveness on the part of investors and shareholders to know the finally adjusted standard profits of companies has considerably increased; for it enables one to judge the dividend prospects of a company much more accurately than before. There has been a demand that the leading financial journals of the country should publish periodically the last adjusted standard profits of leading companies, the shares of which are quite popular on the different stock exchnges. But the management of companies prefer to be silent on this question. While some take at least their shareholders into confidence, the majority of them seem to be reluctant to do even that; nor do they give any indication whatever of such in their directors' reports.

There does not appear to be any compelling reason why company managements should withhold this essential information at least from their own shareholders if not from the investing public generally. Mr. K. R. P. Shroff, President of the Bombay Stock Exchange, in his speech at its annual general meeting held on 6th May 1944, referred to this point. He said that some companies outside the Bombay Presidency, for instance, the Cawnpore Sugar Works, Ltd., had of their own accord, circulated such information amongst their shareholders and he was of the opinion that managing agents of companies in other provinces should also follow this commendable example. He revealed that the efforts of his Exchange to collect reliable information by making a direct approach in the matter to company agents had not met with encouraging response. He felt that the withholding of such vital information from shareholders and the investing public required an explanation. In the meantime, he urged shareholders to compel the managements of companies in which they may have holdings to disclose the relevant statistics and thereby help in protecting the interests of the class to which they belonged. *The Commerce* dated 13th May 1944.

*(c)* **Reserves.** These have already been discussed in a previous chapter.

3. **Relation between Profits and Dividends.** The dividends to shareholders should be decided from the point of view of profits earned and the future outlook of the company. From the profits earned the essential provisions for depreciation and taxation must first be made, and then as much as possible should be allocated to desirable reserves with a view to strengthening the financial position of the company, before the amount available for distribution is settled. "The policy of sacrificing its dividends to its reserves is the one which every company whose financial situation permits should follow. In no other way can a company whose permanent earning power is doubtful so certainly raise its securities to an investment position as by adherence to the policy of accumulating large reserves out of profits. In no other way can a company whose capitalisation is excessive compared with its earnings, justify that capitalisation save by 'ploughing in' its profits, making the crop of earnings grow up into larger harvests of revenues. *"Mead"; Corporation Finance.*

In fixing the rates of dividends, the following rules may serve as a guide :—

*(i)* **Stability of Dividends.** It is very desirable that the dividend paid year after year should be as far as possible uniform. That is the view now held by prudent directors of companies. In the distant past

the practice was to regard shareholders as standing in substantially the same relation as partners. They were supposed to be familiar with the status and fluctuations of the business and were expected to share in its ups and downs. If the enterprise enjoyed an exceptionally good year, it was accepted as a matter of course that the dividend rate would be correspondingly increased. If in the following year there was a sharp decline in profits, the dividend rate should be correspondingly cut. As a matter of fact this is today the practice of a great number of companies.

So long as the practice of fluctuating dividends is followed by private companies and companies in which the public is not substantially interested, there can be no serious objection. In fact section 23-A of our Income-Tax Act encourages this practice. In such companies the shareholders themselves take an active part in the business and are familiar with its very phase.

But the companies which have shareholders who are not active in the business or familiar with its activities are in a different position. The great majority of the shareholders of such companies have only the barest information as to the manner in which the business is handled and as to the results that are being achieved, and are not sufficiently familiar with the business or sufficiently interested in it to absorb more detailed information if it were given to them. They regard their ownership of a company's shares merely as an investment of capital that will bring them an income.

**Advantages of stable dividends.** The interests of both the shareholders and the company demand that a rate of dividend once established shall be maintained. The shareholder desires a stable dividend because the value of a share whose dividends for example, are *6, 6, 2, 2*, and *4* averaging 4 per cent. for the five years, but irregularly distributed, will command a lower price than the shares on which 4 per cent. is paid every year. Investors, as distinct from speculators, desire stability in the income from their investments. The dividends which they receive go into their personal income accounts ; their expenditures and appropriations are adjusted to these receipts ; a reduction or the passing of a dividend disturbs their calculations and reduces their confidence in the company. As a result of this preference of the investor for shares with a regular rate of distribution, the payment of regular dividends produces a higher and more stable value for such shares. Shares with regular dividends are worth more to sell and are also more valuable as collateral security.

A stable rate of dividend with its resulting higher and more permanent market price is also of great advantage to the company. Many companies have to borrow for current finance ; and in order that a company should retain a strong position with the banks, it is important that its shares should be maintained at a good figure, because the bank considers it good evidence of the financial standing of the company applying for a loan. A settled market value for its shares which can be obtained only by stabilising its dividend rate also benefits the company because it makes it possible to procure, on more favourable terms, money for improvements and extensions. A prosperous company is usually a growing company, and is under frequent necessity of selling shares or debentures. The prices obtained for the new securities will depend upon the prices of those already outstanding.

*(ii)* **Cumulative Preference Dividend.** The issue of cumulative preference shares seriously interferes with a conservative management of a company's earnings. It is true that the directors are not bound to pay the preference dividends unless their judgment so dictates. The ordinary tests of policy apply to dividends on preference as well as ordinary shares. The company must have the necessary reserves and be able to spare the cash. If no dividends are to be paid on ordinary shares, the directors may pass the preference dividend as well and plough back the entire profits. This policy has the advantage that no interest is payable on the arrears of preference dividends during the period of default. If arrears go on increasing, they may be funded and never paid in cash, as is usually done in any financial reorganisation, e.g., the reorganisation scheme of the Kumardhubi Engineering Co, Ltd., put through in 1943.

While there is left a much larger measure of discrection to the directors who may decide to defer the payment of preference dividends, there is a corresponding penalty in the fact that the accumulated dividends constitute a growing barrier in the way of ordinary share dividends and that the credit of a company is adversely affected by piling up large arrears of preference dividends. For these reasons, companies that are earning sufficient profits and are in sufficiently strong financial condition usually pay their preference dividends without much argument.

*(iii)* **Initial Dividends.** A new company need not be in a hurry to start paying dividends, and the rate of the maiden dividend should be *fairly low* in order *to* guard *against future contingencies. Every* new company is an experiment. Even if it belongs to an established industry, the extent of its success cannot be correctly predicted. In every business there are a number of unknown factors, viz, new laws to reduce profits, e g, excise duty; increase in taxation; increased competition; changes in tariffs; industrial depression; demands of organised labour; substitution of new products; etc. Further, in some companies, particularly those formed during a boom, there is some overvaluation of the property purchased and a corresponding element *of inflation in the capitalisation*. Even with the most pains *taking* care, mistakes of construction, location, or anticipation of demand may have been made.

*(iv)* **Fluctuations in Earnings.** The earnings of a company are the coefficient of three factors: (i) The volume of sales; (ii) Selling prices; and (iii) The cost of production. Business does not always move on an even keel. Economic and financial conditions vary; changes in management occur; difficulties with employees arise; changes in taste may suddenly create new markets or wipe out existing ones—all these and many other factors which are constantly at work bring about kaleidoscopic changes which often come as great surprises even to people who are intimately acquainted with business. It is therefore sufficient to note that profit fluctuations do exist in all businesses, and that they must be reconciled with the necessity of paying a regular rate of dividend, a rate which changes only to increase.

In view of the fact that earnings are usually bound to be irregular, it is impossible for many directors to pay out all their profits to shareholders without making dividends unstable and damaging

the financial standing of the company. To reconcile the necessity of stable dividends with the fact of unstable profits, the directors must pay out only such a percentage of profits as will leave a margin over the dividend requirements, assuming profits to fall to the lowest point which, in all reasonable probability, will be reached. Directors ascertain from their own experience and from the experience of other companies similarly situated what are likely to be the lowest earnings under the most unfavourable circumstances, and then fix its dividend rate well below that point. In order to maintain a rate of dividend, a company should have its maximum dividend requirements always fall below its minimum earnings If the opposite policy is adopted, large profits will be paid out of large profits, small dividends out of small profits, and the value of the shares will be low and uncertain. Mead: *Corporation Finance.*

*(v)* **Bonus.** The rate of dividend in a really stable and well-managed company is not increased unless the directors have satisfied themselves that in all human probability a later decrease will not become necessary. If there are unusual or possibly temporary profits, which it is thought wise to distribute the directors will ordinarily announce an extra dividend called *'bonus'*, for whose continuance there is no guarantee.

This point is well illustrated by the dividend policy of the Muir Mills Co., Ltd., which distributed dividends for the last five years as follows :—

| | 1943 | 1942 | 1941 | 1940 | 1939 |
|---|---|---|---|---|---|
| Preference Dividend | 6 | 6 | 6 | 6 | 6 |
| Ordinary Dividend | 20 | 20 | 20 | 20 | 20 |
| Bonus to ordinary shareholders | 50 | 30 | 10 | 5 | 3 |

From these figures it is obvious that the directors have been consistently maintaining the dividend at 20 per cent. per annum, while progressively raising the rate of bonus to shareholders in consonance with the rise in the profits of the company. This procedure is of course in strict compliance with the more orthodox system of finance and serves to remind the shareholders that the continued rise in profits is only of a temporary nature and that such should not be counted upon to last for an indefinite period. *The Commerce* dated 12 February 1944.

The bonus may be converted into ordinary dividend only when the directors of a company feel that prospects for it are good and that there would be no difficulty in maintaining the dividend at the increased level in the next few years.

*(vi)* **Cut in Dividends.** If the profits of a particular year do not justify the payment of the usual dividend and if there is no certain hope of future improvement in the profits of the company, there should be no hesitation in curtailing the dividend, because in that case the theory of maintaining the regular dividends, would be unsound.

To take an example, the jute industry in India was faced with a number of difficulties in 1943, and the earnings of nearly all jute mills suffered a serious set back in that year. Therefore most of the

well-managed jute mills cut down their dividends for 1943 to suit the profits earned, and did not resort to the policy of drawing upon the reserves just to maintain the dividend level, although they were in a position to do so. This shows that the managements of these companies were quite aware that the setback suffered by the industry in 1943 had not been of a type to justify a draft upon reserves in order to remunerate the capital at the previous high level.

The same healthy principle of cutting down the dividends to suit the profits earned was followed by the Associated Cement Companies, Ltd., in the distribution of its profits for the year ended 31st July 1943. Some of the shareholders present at the seventh annual general meeting of the Company held in January 1944 stated that the reduction in the dividend level was not justified and that the Board ought to have maintained it at the previous year's level by reducing the transfers to reserves and depreciation. One shareholder went to the extent of suggesting that dividend should be maintained at a steady and uniform level as the cement industry had come to be ranked with public utility companies. In replying to these remarks, Sir H. P. Mody, the Chairman of the Company, rightly stated that he could not subscribe to the view that dividends should be maintained merely for the sake of uniformity without paying due regard to the position of net profits. Net Profits and dividends, he said, must be related to each other. Proceeding, he said that the maintenance of dividend by a company in a year in which profits were less would be justified to a certain extent if there was some assurance that in the following year, at least, the earnings would improve and thereby provide an opportunity to make up the deficit in the essential transfers that might be necessitated in order to maintain the return to shareholders. But in the case of the A. C. C. there was up to that date, he said, no such assurance. *The Commerce* dated 22 January 1944.

*(vii)* **Draft upon Past Profits.** If the decline in the earnings of a year is considered by all means to be temporary and there is every likelihood of an improvement in future, there can be some justification for drawing upon the past profits ( reserves and carry-forward ) for the purpose of maintaining the usual dividend.

Frequently the question arises whether dividends which have not been earned during a given period should nevertheless be paid and charged against the reserves that have been accumulated in previous periods. Ordinarily the answer is no. As a rule the reserves form a part of the permanent capital of the company much in the same way as share capital, particularly when they have been expended in acquiring capital assets and are not represented by liquid resources. In such circumstances they are not available for dividend purposes.

*(viii)* **Interim Dividends.** The term 'interim dividend' means a dividend paid to the members of a company in anticipation of the profits of a period before the accounts of the company for that period have been prepared, audited and adopted by it at the ordinary general meeting. In other words, an interim dividend is a dividend declared at any time between two ordinary general meetings. Interim dividends are declared by directors who are empowered to do so by the articles of companies When an interim dividend or dividends have been paid, any further distribution to shareholders, sanctioned in a general meeting

on the recommendation of directors is called 'final dividend'. Where the articles provide for the payment of interim dividends, a mere resolution of the Board of Directors to pay does not create a debt as between the company and the shareholders and the directors are entitled to rescind the resolution subsequently, before the dividend is actually paid off.

Quite a large number of companies in India (particularly jute mills, coal mines, light railways companies and some banks) prepare their accounts half-yearly, hold half-yearly ordinary meetings of shareholders and declare half-yearly dividends. In such cases, the dividend paid after the first half-year cannot be called interim, because it is paid after the closing of the books and is sanctioned by the general meeting.

On the other hand, during the recent war owing to the uncertainty of mails, the preparation of the accounts of some companies (e g., those having foreign interests) was delayed Such companies declared an interim dividend in the usual way and also declared a second interim dividend before the closing of the books. The second interim dividend was given in place of the final dividend in order to enable the shareholders to receive it without unnecessary delay, which would otherwise have been caused by the closing of the books and the holding of the ordinary general meeting. This war-time practice relating to the payment of a second interim dividend was referred to by the Chairman of the Indian Iron and Steel Co , Ltd., in his speech at the annual general meeting held on 19th December 1941 in the following words :-

"Your Board has followed the practice initiated last year of making a final dividend distribution by means of a second ad interim dividend so as to enable payment to be made at the usual time in september which would otherwise have been Impossible in view of the delays of communications between India and the United Kingdom. These delays will, I am afraid, continue during the present state of world upheaval."

Owing to the exceptional war-time prosperity, a few companies in India have paid in recent years more than one interim dividend in addition to the final. The Cambodia Mills, Ltd., paid for 1943 the first interim dividend of 10% in June 1943 and the second Interim dividend of 10% in October 1943. It also declared at its annual general meeting held on 28th March 1944 a final dividend of 50%—thus making 70% for the year. The Be Be Rubber Estates, Ltd., paid for the year ended 31st March 1943 three interim dividends for that year amounting to $7\frac{1}{2}$%, 5% and $2\frac{1}{2}$% respectively. No final dividend was, however, recommended, but the last interim of $2\frac{1}{2}$% constituted the final. It was styled as the third interim dividend because books had not been closed at the time it was paid. The Patrakola Tea Co., Ltd., paid for the year 1942 the first interim dividend of 10% in November 1942 and second interim dividend of 10% in February 1943, and at its annual general meeting held in June 1943 it declared a final dividend of 75% thus making 95% for the year.

Considerable responsibility rests with the directors of a company when they decide to pay an interim dividend; and before doing so they must take the following precautions :—

(a) The profits made by the company must be carefully estimated. For this purpose it is advisable to prepare interim accounts for the half-

year. The directors of Sri Krishna Rajendra Mills, Ltd., Mysore, declared on 13th February 1944 an interim dividend of Rs 1·80 per share; but before doing so they had the account of the Company prepared for the half-year ended 31st December 1943 and the accounts were also audited. Where, however, the business is of such a nature that the percentage of gross profit on turnover is more or less constant year by year and there are no unusual factors during the current year which may affect the figure of profits, it may be possible to dispense with the taking of stock and the preparation of interim accounts, because the gross profit for the half-year can be computed at the usual percentage on the sales for the period; and then by deducting from the gross profit the actual expenses and the necessary provision for outstanding liabilities, depreciation and contingencies, the net profits for the period may be estimated.

(*b*) A careful inquiry should be made into the conditions of trade and the prospects for the remainder of the year because it is quite possible that the profit earned during the first half-year may be swallowed up by a loss in the second half-year.

(*c*) The company's cash position should be examined, since it would be inadvisable to pay an interim dividend, although there may be profits, if such payment would unduly deplete the working capital of the company. In this connection it is important to ascertain whether the company has any future financial commitments, e.g., funds may be required in the near future for the payment of liabilities, for financing capital expenditure, etc. If so, the payment of an interim dividend would not be justified.

(*d*) If it is decided to pay an interim dividend the rate fixed should be lower than the estimated rate for the whole year, because it is better that the final dividend should be higher than the interim.

When an interim dividend has been paid, it is not necessary that there should always be a final. Circumstances may render the payment of the final dividend inadvisable or the circumstances may require that the final dividend may be satisfied otherwise than in cash. The Singareni Collieries, Ltd., Hyderabad (Deccan), paid in January 1943 an interim dividend of 2½% for the year ended 31st December 1942, and it was the directors' intention to recommend a final dividend; but the Company was required by the British Indian Income-Tax Authorities to furnish a return of income from the tax year 1939-40 to that date, and until it could be ascertained what liability, if any, to income-tax existed, the directors did not consider it would be in shareholders' interests to recommend the payment of a further dividend in view of the complications which might ensue should the company be held liable. The Shri Niwas Cotton Mills, Ltd., paid in 1943 on account of the year an interim dividend of 10%, but it did not declare any final dividend, although there were sufficient profits carried forward, because it thought it prudent to husband its cash resources in view of the immobilisation of the entire excess profits by the Indian Finance Act of 1944 In lieu of a final dividend, it declared in June 1944 a 20% capital bonus out of the reserve fund and issued in satisfaction thereof 4,800 4 per cent fully paid-up cumulative redeemable preference shares of Rs. 100 each which are redeemable at par at any time after 31st December 1949 by giving six calendar months' notice.

4. **Cash (or Ways and Means) Position.** In discussing the relation between profits and dividends, it has been assumed that adequate and regular profits justify dividends. But this assumption should not be allowed to remain unchallenged. It is, in fact, the direct source of a large number of financial embarrassments. Many companies which have been able to report highly satisfactory profits and which have paid decent dividends on the strength of those profits, have found themselves—to the utter surprise and indignation of their shareholders and even of their directors and managing agents—in financial difficulties. It is quite apparent that many business men do not grasp the fact that dividend payments should be dependent not only upon profits, but also upon the company's cash position.

It is needless to emphasise that many companies find their chief financial difficulties arising not in periods of depression and declining business but in their periods of prosperity. To attempt to do a large volume of business with a small working capital is one of the quickest and surest methods of financial hari-kari. Yet, this is precisely the course that is followed by those concerns which, on the strength of a showing of profits, declare dividends, the payments of which seriously depletes their working capital. Under these circumstances the only prudent course is to withhold dividends until in the normal course of the company's business cash is accumulated beyond the requirements of the business. It is not merely a book profit, but in addition a satisfactory cash balance that should furnish the basis for a declaration of cash dividends. Longh : *Business Finance*.

**Alternatives.** Where a company is not in a position to spare cash for the payment of dividends, because the growth of business may have needed larger stocks of stores, raw materials and finished goods, larger book debts or new facilities, the best policy to be pursued is, of course, to pass dividends; but this course may not always be advisable having regard to the effect it may have on the market price of its shares. Under such circumstances the company may have recourse to the following alternatives :—

*(a)* **Borrowed money.** The directors may decide to borrow money for the purpose of paying dividends. This may be the case with companies which have to contend with wide seasonal fluctuations and with companies which normally operate with a small working capital. The public utility companies usually belong to this group. For companies of this type it may not be an unsound financial policy at times to pay dividends with the proceeds of temporary bank loans, assuming, of course, that there can be no reasonable question as to the company's ability to repay, these loans, without crippling itself. Thus where the company's profits have been used as temporary additional working capital and are locked up in book debts and stock which will be realised in the near future, the money required for the payment of dividends may very well be raised by means of bank loans, because when book debts and stock are realised, the bank loans can be easily paid off.

*(b)* **Issue of Further Capital.** The funds required for the payment of dividends may be raised by issuing shares ; but this is a method which may be adopted only in very exceptional circumstances, because thereby the company's ability to maintain future dividends on the increased

capital will be considerably impaired If a company follows this practice during a period when it is not making a legitimate showing of profits it would be clearly engaged in a fraudulent transaction. But if it does so during a period of adequate profits, its action is not necessarily fraudulent, but it is certainly not a sound one. Lough. *Business Finance*

*(c)* Issue of Redeemable Preference Shares or Debentures. Where the profits of a company have been used for financing block expenditure, it is not desirable to pay dividends by temporary borrowing from the bank, because it will not be convenient to repay the bank loan. In such circumstances the funds raised must be of a more or less permanent nature and the issue of redeemable preference shares or debentures repayable after a few years may be quite suitable for the purpose, if the company is going to make provision for their redemption by means of a sinking fund created out of profits.

*(d)* Scrip Dividend If cash is expected in the near future, scrip may be issued. Scrip dividend is one which is satisfied by issuing to the shareholders the company's promises to pay. Such promises may or may not bear interest. They usually mature at some definite date, but may be redeemable at the option of the company with a certain limit of time. The scrip dividend may be issued by a company which has made a good showing of profits during a given period but is not insufficiently strong financial position to part with cash, and it is not considered prudent to resort to borrowing, and at the same time it is desired not to spoil a dividend record.

The scrip dividend is satisfied by issuing deposit certificates, deferred dividend warrants or income stock certificates.

The best example of a scrip dividend is furnished in India by the Tata Iron and Steel Co., Ltd., which on the recommendation of its directors, declared in July 1942 an additional dividend of Rs. 12 per ordinary share and an additional dividend of Rs. 86 per deferred share to be satisfied in both cases by the issue of bearer deposit certificates bearing interest at 3% per annum redeemable at any time at the Company's option within three years from the 10th August 1942.

This policy of the Company was criticised by the shareholders on the ground that

*(a)* It was novel ;

*(b)* The required amount could easily have been borrowed from Banks and the dividends paid in cash ;

*(c)* It adversely affected the credit of the Company ; and

*(d)* The Agents had failed in their duty to provide finance.

These criticisms of the shareholders were completely and satisfactorily answered by the Chairman of the Company, Mr. J. R. D. Tata, at its annual general meeting held on 30th July 1942 ; and the relevant extracts from his speech are reproduced below :—

"A feature of this year's dividends which has aroused a certain amount of controversy is the Directors' recommendation to pay a part of the dividends on Ordinary and Deferred Shares in the form of bearer deposit certificates. In the course of correspondence with the

Shareholders' Association and in a statement issued to financial newspapers, the Managing Agents have explained at some length the purpose and objects of this scheme and the reasons for its necessity. As some of the shareholders present may not have had an opportunity of reading these statements and as it will help to shorten discussion later during the meeting, I shall do my best to answer now the criticisms levelled against the scheme and summarise the arguments in its favour.

"The scheme has only one object; namely to conserve the Company's resources at a time of emergency and impending danger, and when its ways and means position has begun to show signs of deterioration.

"The two principal criticisms made against the scheme have been on the grounds that it is unncessary to conserve resources at this stage and that if additional cash is required, it can and should be borrowed from Banks. The scheme has also been criticised on the grounds that it is novel and unprecedented, that it will adversely affect the credit of the Company and that the Agents have failed in their duty to provide finance for the Company.

"Let me first answer the last three arguments The novelty of a measure should not constitute a sufficient ground for its condemnation it is otherwise sound, as this one most certainly is The whole situation in the world to day is abnormal and unprecedented and provides ample justification for the adoption of exceptional or unprecedented measures.

"Your Directors cannot agree that the credit of the Company has been at all adversely affected by the announcement of this scheme. On the contrary, the fact that the Company has given this clear indication of its determination to strengthen its ability to face any emergency should raise rather than lower its credit and prestige in the eyes of the public. Its position vis-a-vis the Government of India will certainly be enhanced by it and, should circumstances unfortunately arise which would necessitate its turning to Government for help, the Company will have a better case and will receive a more sympathetic response than if it had made no effort to conserve its resources when it could.

"Your Agents have shown that they are fully alive to their duty to provide the necessary finance to the Company as far as it lies in their power to do so. May I remind you that in fulfilling this duty in the past, when the Company was passing through a grave financial crisis they did not hesitate to sacrifice 25% of their commission in perpetuity. Even to day, they have guaranteed the cash credit arrangement for One Crore of Rupees with the Imperial Bank. Although it is sparsely used at present, and although the credit is backed by substantial liquid assets, a situation might well arise in critical times like these when, with stocks frozen, this guarantee would become a personal liability to be met by the agents out of their own resources The Agents have now voluntarily offered to deposit with the Company, free of interest and for so long as the certificates remain outstanding, a substantial portion of their commission for this year. If they have recommended to the Board this scheme for the partial payment of dividends by the issue of certificates, which was unanimously accepted by all the Directors,

they have done so in the discharge of their duty to ensnre the safety and stability of the Company.

"I shall now deal with the two mnre important criticisms mentioned above, the first being that the scheme is unnecessary under present conditions. This is a criticism which would he quite reasonable if the scheme had been proposed in normal peace time, but it totally ignores the state of emergency which exists in the country to day as a result of the war. The entry of Japan into the war last December, and the subsequent developments of which yon are all aware, have created a grave situation for the Company by bringing it well within the zone of danger. To some nf yon nn this side nf India, the war may appear to be remote, bnt to those in Jamshedpur, who are sitnated within easy bombing range of the enemy and to those of ns here who are directly concerned with the operations nf the Cnmpany, the safety of its plant and the welfare of Its employees, the sitnation is one of constant and acute anxiety.

'Besides the danger of direct damage to Jamshedpnr, other serions factors rising from the war threaten the operations of the Works and the earning power of the Company. It may be recalled, for instance, that earlier in the year there was a large exodns of labour from vulnerable indnstrial areas, particularly in Bengal and Bihar. Although the situation at Jamshedpur was kept under reasonable control thanks to the prompt measures taken at great cost by the Company to protect and reassure its workmen, the possibility of the recnrrence of such a movement at Jamsedpnr, on the coalfields or on the railways, cannot be rnled out and It will then undoubtedly be on a mucb more serious scale if it is caused by a direct attack on India or by the bombing of Jamshedpnr and other key points. Apart from this very potent factor the dislocation of transport in the country and a number of restrictions necessitated by the war have already begun to hamper production In our plant.

"In these circnmstances and in the light of a future so uncertaio can it be said that the need bas not arisen for the Company to make every effort to strengthen its resources to meet a possible emergency should it unfortunately arise?

"The next question that mnst be considered, therefore, In completing the answer to this particular criticism is whether the existing resources of the Company are adequate to meet snch an emergency. The answer is that they are not. Although there has been during recent years a substantial and continous improvement in the financial position of the Company, as pointed ont in my previous speeches, the liquid resources at our disposal to day are barely sufficient to meet the very heavy demands that will be made on them upto the end of the financial year. They would be all the more inadequate to meet an emergency which might dry up the Company's sources of income and freeze the assets against which it conld borrow. The financial operations of this Company are of such a magnitude and complexity that any sndden interruption or dislocation of the flow nf receipts and outgoings would in a very short while cripple its ways and means position.

"The remaining material criticism to be answered is the suggestion that if the Company needed additinnal cash it could easily have borrowed it from the Banks or the public. That is an obvions criticism

which, like the previous one, would have been valid in normal times. It would undoubtedly be an easy matter for us to borrow the required sum, but that would hardly conserve our resources. The extent of the Company's borrowing capacity is determined by the assets it can offer as security. To-day our borrowing capacity is considerable, but if a serious emergency were to arise it would be greatly reduced at the very time when we would need to borrow most. The sum which the shareholders will leave with the Company as a result of the issue of certificates in lieu of cash, together with the sum which the Agents have offered to place at the disposal of the Company without interest comes to well over a Crore of Rupees. If the Company were to borrow such a sum today, it would merely impair its future credit to that extent. The present scheme, together with the Agents' offer, will therefore result in conserving the Company's future capacity to borrow at a much higher level than would be the case if a loan of a Crore was, as suggested, taken from the Banks at this stage.

"If we accept, as we must, the position that it is necessary for the Company to conserve its cash resources and also its capacity to borrow in the future, what are the means at our disposal to achieve that object and meet our present ways and means requirements? Our day to day operating expenses must be met as they occur while our other commitments such as taxes, war insurance premia, dividends, agents' commission, profit-sharing bonus etc., cannot be postponed for any length of time. The only practical means, therefore, by which the Company can conserve its cash is to distribute less of its profits to its shareholders and employees, and the simplest method of doing so would be to declare a much smaller dividend and bonus This, however, would cause both our shareholders and our employees great hardship and it is because they wish to avoid this that the Directors have recommended the present scheme which reconciles the reasonable expectations of the shareholders and employees with the need for conserving cash. It can hardly be doubted that the shareholders would prefer to receive part of a larger dividend all in cash, particularly when facilities have been announced by a number of Banks which will enable those shareholders who need money to convert their certificates into cash immediately and without loss or cost."

*(e)* **Capitalisation of Profits.** Where a company possesses large profits—past profits in the shape of reserves as well as current profits—and it desires for certain financial reasons to distribute to the shareholders a special dividend out of them, it cannot possibly pay a huge cash dividend. A special dividend or bonus is therefore declared and satisfied by the allotment of shares or debentures of the company. Where the issued capital of the company is only partly called up, the bonus may be applied towards making the shares fully paid. Thus the profits which are distributed in the form of capital bonus become permanently a part of the company's issued capital or debentures, and this process is known as the "Capitalisation of Profits," and the shares or debentures so allotted are called 'bonus shares' or 'bonus debentures'.

**When Capital Bonus is Warranted.** The policy of issuing bonus shares leads to an increased dividend-bearing capital of the company, and the company may not be able to maintain its regular dividend on the expanded capital. If bonus shares are issued merely because

for want of sufficient liquid resources a cash dividend cannot be paid, it is not a sound financial policy, because in that case increased future profits are not assured. In want circumstances then can the issue of bonus shares be warranted if judged by the canons of good finance ? The circumstances are as follows :—

*(a)* When reserves grow to a size which in the opinion of the directors is not justified by contingencies which may make a call upon the company's resources, they may be distributed as bonus shares.

The Mysore Spinning and Manufacturing Co, Ltd., had on 29th February 1944 paid-up share capital Rs. 14,86,410 and reserves Rs. 45,94,060 that is to say the reserves were more than three times the paid up capital. With a view to strengthening the financial position of the Company the directors proposed to increase the authorised capital from Rs 15 lakhs to Rs. 50 lakhs by the creation of a further 30,000 ordinary shares of the face value of Rs. 50 each and 40,000 preference shares of the face value of Rs. 50 each, and to issue as fully paid-up 14,901 cumulative preference shares by capitalising Rs. 7,45,050 out of the reserve fund of the Company. These cumulative preference shares will carry a fixed preferential dividend of $4\frac{1}{2}\%$.

*(b)* When the reserves built up by a company have been expended for purchasing revenue-producing assets, and there is a wide gap between its share capital and the block account, since in that case the position is the same as if dividends had been paid in cash and new capital had been issued to provide for the acquisition of those assets.

The Balance Sheet of Ahmedabad Manufacturing and Calico Printing Co., Ltd., on 31st December 1940, showed paid-up share capital Rs. 29,99 770 ; Reserves Rs. 38,00,000 ; Depreciation Fund Rs 87,19,994 ; and Gross Block Rs. 1,75,60,567. In other words, the reserves were used for purchasing the revenue earning fixed assets. In March 1941, the issued capital of the Company was increased to Rs. 41,00,000 by the capitalisation of Rs. 8,00,000 out of the Depreciation Fund and creating thereby 16,000 $4\frac{1}{2}\%$ (taxable) cumulative third preference shares of Rs. 50 each These shares were issued free to the existing ordinary shareholders in the proportion of one such share for every share held.

*(c)* When there is any other factor contributing to the improvement in the future earnings of the company, e. g , saving in interest charges owing to the repayment of outstanding debentures.

The Directors' Report of the Elgin Mills, Co., Ltd., for the half-year ended 30th September 1943 contained a proposal for the capitalisation of a portion of the general reserve, which had received the sanction of the Government of India under the Defence of India Rule 94A. The proposal arose directly from the redemption of debentures of the value of Rs 10 lakhs, which had matured on 30th September 1943. The Company used to set apart year after year a certain sum out of the profits to a debenture sinking fund which was invested in readily. marketable securities. These investments were realised and the debentures duly paid off on the redemption date. The sum of Rs. 10,32,204 standing to the credit of the debenture sinking fund, therefore, had become free and this the directors had

disposed of by utilising Rs. 5,00,000 in writing down Goodwill and by transferring the balance to General Reserve.

As a result of this transfer of Rs. 5,32,204 and as also of the amount of Rs. 4,87,776 earmarked out of the profits for the half-year ended 30th September 1943, the General Reserve had become richer by Rs. 10,19,980 in one half-year. With such a large addition the General Reserve stood at Rs. 32,20,000. It was out of this that the directors proposed in December 1943 to capitalise a sum of Rs 4,20,000 by the issue of one fully paid-up 5% (tax-free) 'B" cumulative preference shares of Rs. 10 each for every five ordinary or vendor shares held, as a capital bonus, which was to rank for dividend with the existing shares as from 1st October 1943.

With the redemption of debentures and the writing off of Goodwill the bonus shares cannot in any way affect the future dividends on ordinary and vendor shares, as the prior charge on account of the new preference capital is only Rs. 21,000 while the saving on account of debenture interest is as much as Rs 70,000, and further as there will be no necessity in future to write off Goodwill.

*(d)* When the capital bonus is satisfied by the issue of low-dividend and redeemable preference shares of the company. This is a clever arrangement to enable the shareholders to participate in the increased profits of the company without at the same time reducing its liquid resources, and the option taken by the company to redeem the bonus preference shares provides for an automatic reduction of the share capital out of profits.

The Shri Niwas Cotton Mills, Ltd., paid in 1943 on account of that year an interim dividend of 10%; but the directors thought it prudent with a view to husbanding its resources on account of the immobilisation of the entire excess profits by Government not to recommend the payment of any final dividend for that year, although there were enough profits available for that purpose. In lieu of a final dividend, the Company declared in June 1944 a 20% capital bonus, out of the reserve fund and issued in satisfaction thereof 4,800 4% fully paid-up cumulative redeemable preference shares of Rs 100 each which are redeemable at par at any time after 31st December 1949 by giving six calendar months' notice. The option taken by the Company to redeem the bonus preference shares within such a short period renders the whole arrangement more or less similar to the issue of deferred dividend certificates obviating at the same time the disadvantage of the shareholders having to pay heavy war-time taxation

**Advantages and Disadvantages.** The following are the advantages and disadvantages of the policy of issuing bonus shares :—

**(a) From the point of view of the company.**

1. Profits can be distributed without any distribution of the company's assets. The company is thus enabled to conserve its liquid resources which provide additional working capital for its present and future needs.

2. Where the reserves have been utilised for financing fixed capital expenditure, the issue of bonus shares reduces the disparity

between the paid-up share capital and the block account of the company, and the Balance Sheet reflects the company's true position.

3. The issue of bonus shares, in lieu of a cash dividend does not add to the existing purchasing power of the community, and is, therefore, an anti-inflationary measure.

4. By capitalising profits the dividend is maintained at or reduced to a level more correctly representing the real earning capacity of the company, and this fact protects the company against the appearance of the prosperity much in excess of that which it has actually achieved. In these days of E. P. T. and the growing labour demands that is no small consideration.

5. Unless there is a sufficient increase in the future profits of the company, the increased issued share capital is bound to reduce the rate of future dividends, and this may cause discontent amongst the shareholders. But, if the bonus is satisfied by the issue of preference shares, the dividend bearing capital of the company will not become too unwieldy as the return payable on the new shares will be limited, and the future rate of distribution to the ordinary shareholders will not be affected to any material extent.

*(b)* From the point of view of shareholders.

1. The shareholders receive the profits without in any way affecting the company's cash position; and they can, if they so desire, convert these shares into cash by sale on the market, usually at a considerable premium, because the issue of bonus shares has a very favourable effect on the market price of the company's shares.

2. It is true that the issue of bonus shares does not enable the shareholders to get a regular cash income; but they stand to gain ultimately. With the purchasing power of money being so low at the present time, the real income by getting cash dividends now will also be lower. Instead, if the shareholders allow such income, as they are entitled to, to be utilised for increasing their right on the capital of the company they stand to gain in three ways:—

*(a)* They are given an opportunity to invest their income in a first-class industrial scrip which they cannot hope to get in the market except at a high premium;

*(b)* They do not suffer any loss in their real income owing to the present fall in the purchasing power of money; and

*(c)* They will not be paying any super tax which they would have to pay on a cash dividend.

3. Unless the company makes increased profits, a reduction in the rate of future dividends will depress the market price of the company's shares and a shareholder wishing to sell his shares will suffer capital loss.

4. The issue of bonus shares may encourage speculative dealings in the company's shares, thus causing wide fluctuations in their market value.

The whole position discussed above may now be summed up as follows :—

Good company finance is that which places a company in the happy position of having valuations approximating to its true assets; a reserve sufficient to meet possible contingent liabilities and to equalise an unexpected bad period with the normal; capital adequate to the needs of an expanding business, and an earning power sufficient to allow for a good dividend; a wise allocation to reserves, and special allocations to funds which tend to increase the goodwill and stablise the prosperity of the enterprise, in which category we must today include staff pensions and welfare expenditure.

Company finance which allows too wide a variance—either way—between balance sheet and actual valuations, which allows reserves and provision for depreciation to suffer in favour of dividends, or which too frenziedly accumulates such provision at the expense of the members of the company, is not good It is, of course, preferable that a company should err on the side of guarding the future at the expense of the present than that of feeding the present at the risk of the future; but error either way reveals a lack of financial balance in the minds of those responsible, caused in one case by too cautious and in the other by too sanguine a temperament. Brooks: *Theory and Practice of Finance*

**Dividend Policy of Companies in India.**

A few years before the recent War, *Indian Finance* in its Investors Supplement dated 14 March 1935 wrote an article under the heading 'Clive Street Finance Sound but not Correct.' This article described clearly the dividend policy of our companies and is reproduced below in extenso.

"It is a common charge that, in the generality of cases, Bombay Cotton Mills, in extravagant dividend distribution, frittered their profits of prosperous days and that this is the main reason why they were specially unfitted and incapacitated to meet the depression There is a great deal of force and truth in this charge. The Bombay Mills exploited the present and debilitated the future.

We venture to bring a no less grave charge against the Calcutta companies that, by stingy dividend distribution and by extravagant allocations to depreciation and reserve, they deprive the present shareholders of their just dues. They seek to benefit the future generation of shareholders at the heavy sacrifice of the present.

What is needed is a sense of proportion—a balanced plan of action.

We may give off hand a few instances. The block of Gourepore which owns 1392 looms stands in the books at Rs. 4.86 lakhs, The original block cost was Rs. 161.25 lakhs. The depreciation provided from profits is the stupendous sum of Rs. 156.39 lakhs. Kinnison whose loomage is 1250 and whose gross block value is Rs 97.61 lakhs has a present book value of Rs 17.72 lakhs. Northbrook's original block is Rs. 46.52 lakhs and net block only Rs. 10.87 lakhs. Looms are 567.

'Watchdog' furnished last week the follnwing table in regard to Kumardhubi Fireclay and Silica Wnrks, Ltd. :-

| *Description* | | | *Gross Block* | *Book Value* |
|---|---|---|---|---|
| Land | ... | ... | 94,060 | 15,000 |
| Machinery | ... | ... | 9,22,091 | 1,00,000 |
| Buildings | ... | ... | 10,60,143 | 2,65,000 |
| Kilns | ... | ... | 4,65,652 | 30 000 |
| Siding | ... | ... | 16,689 | 100 |
| Tramway | ... | ... | 3,026 | Nil |
| Furnitnre | ... | ... | 31,428 | 500 |
| Electric Plant | ... | ... | 20,754 | 2,900 |
| Live Stock | ... | ... | 650 | Nii |
| Pipe Line | ... | ... | 16,578 | 500 |
| | | Tntal | 26,32,071 | 4,14,000 |

Fancy machinery of over Rs. 9 lakhs being written down to Rs. 1 lakh ; Kilns of over Rs. 4½ lakhs to Rs. 30,000 ; Railway siding to Rs. 100 : This is depreciating with a vengeance.

Bisra Stone Lime Company spent Rs. 4.91 lakhs on block which is today Rs, 2 lakhs ; machinery and plant cost Rs. 3.53 lakhs and is today a bare Rs. 15,000 in the books. Buildings are written down from Rs. 5.62 lakhs to Rs. 20 000 Tram line costing nearly Rs. 3 lakhs has a net value of Rs. 5,000. Motor cars were bought for a gross value of Rs. 43,958, and its present value of Rs. 500 is mnch more than the value of scrap. Rolling stock at nriginal cost of Rs. 1.32 lakhs is down to Rs. 3,000. Kilns at Rs. 5.88 lakhs are no more than Rs. 1,000. Is this not depreciation run mad ?

India Paper and Pulp passed over dividends because it diverted current profits to the bnilding of the Bamboo plant. Spending current revenue on capital works is the essence of unsoond finance.

Our readers will remember the case of Begg Sutherland's sugar companies in which, in the half-year, the entire damages of the Bihar Earthquake were written off, that is to say, in the same account in which, we were told, the Government have been approached for belp from Earthqnake Relief Fnnds.

As between the Bombay tradition and Calcutta tradition, there can be no doubt that the financial policy of the Eastern Capital is the sounder and better. But this does not prove that the practice pursned here is correct. This policy is sound in that the structure of the company in question is made all the stronger. But the policy is wrong in that the structure is made far too strnng for requirements. He is not a good architect who to make doubly sure uses a beam of ten tons steel where seven tons steel was reqnired.

In any case, the past reserve and depreciation policy has resnlted in the book value of the blocks of Calcutta companies appearing in the current accounts at ridiculonsly low figures and in the accumulation of liquid resources far in excess nf every imaginable contingency ; and the time has come when the further continuance nf this policy must be reconsidered.

We suggest that in the case of companies where depreciation allocations of the past years have brought the book value to much less than a 'true and correct view' of the company's property, no further depreciation should be set aside, nor should any allocation be made to general reserve. The only allocation that will be justifiable is the creation and reasonable accumulation of dividend equalisation fund.

Dividends in the case of Calcutta companies are jumpy. Take the following record of Fort Gloster :—For ten half years (from that ending on 31st March 1930 to that ending on 30th September 1934) it declared dividends of 50, 20, 10, 10, 10, 10, 10, 15, 25, and 30 per cent. If, instead of swelling unwanted reserves and depreciation of block to unjustified levels, the Company had built up and utilised the dividend equalisation fund, the violent vacillations in dividend distribution could have been avoided.

Or take the case of Bisra Lime, Since March 1930 the dividends were in successive half years 60, 45, 40, 40, 30, 30, 30, 40, 40, and 50 per cent.

Calcutta companies have, be it said to their credit, built up their financial structure as prudently and as cautiously as has been built the structure of the premier type of financial institutions, the banks. Let them, also, follow a like dividend policy. Banks do not have jumpy dividends. They use their inner reserves for an even and steady dividend distribution from year to year. Let Calcutta companies create and press into service the dividend equalisation fund towards the same end.

We appeal to Calcutta managing agents to give careful thought to the arguments we have adduced and to the suggestions we have made. We should like one or more of our prominent Clive Street leaders to discuss these issues in the speeches they will make as Chairman at the general meetings of companies.

We hope that our business magnates will not, copying the example of the bureaucrates in the Government, affect lofty superiority to suggestions which in our view are apt to the occasion, and valuable for the fututre of joint stock enterprise in this presidency."

That is what was being done before 1939. Soon after the outbreak of the recent war in September 1939 the Commerce Member to the Government of India made certain statements about the need for conservation of company resources and again in the course of his speech on the Finance Bill in the Central Assembly on 17th March 1941 he recalled his previous warning to industrialists when he said :—

"Let our industrialists and manufacturers remember that this is a good time for them and that once peace is declared, there will be such fierce competition from all manufacturing countries, from countries which are exactly on the same war production basis as ours which will therefore have to turn round and divert their energies to various manufactured commodities, that at that time our manufacturers and industrialists must have something to fall back upon, namely, the resources that they have built now when they are in a position to make profit, when competition is almost entirely shut out, when at least the internal market is completely at their disposal. I raised that voice of caution last time and I repeat it again with even greater emphasis

now, because, as far as I am advised and to the extent that I can personally foresee, the position after the war will be such that all the resources that they have accumulated will be necessary for them. And at that time if any industry, protected or otherwise, has frittered away its resources and is unable to show that it has widely dispensed with all the profits that it has made, no Government will be justified in looking after that industry and giving it a protection which it does *not* really deserve."

In some cases the policy of extravagant dividend distribution not warranted by the profits of a company and its financial position has been due to the fact that the managing agents and directors themselves are largely interested as they happen to hold large blocks of shares. But it may be said to the credit of our industrialists that the warnings thrown out by the Commerce Member have in most cases been taken to heart and the recent war time dividend policy pursued has been on the whole sound.

In these days the management of a company has to decide the dividends to shareholders not only from the point of view of the profits earned and the future outlook, but also from the economic needs of the country as a whole and those of the company itself in the post war period. The complete immobilisation of excess profits, the increase in the rate of taxation (that is to say, in the rate of surcharge from 20 to 24 pies and in the rate of corporation tax from 2 to 3 annas), and the introduction of the system of pay-as-you earn all these have a particular significance and well defined objective, namely, to keep inflation under control. The dividend recommendations of a company management should, therefore, be in consonance with this aim of the Government. *The Commerce* dated 13 May 1944.

The dividend policy followed in the last few years has been usually referred to in the chairmen's speeches at company meetings, and the following extracts from such speeches are of particular interest :—

1. "This year again we have been able to add to our reserve and contingency fund Rs. 7 lakhs, bringing the total figure to Rs. 1 crore and 8 lakhs. The reserve and other funds, including the sinking fund in respect of lands and buildings now stand at over Rs 1 crore and 48 lakhs.

On the year's working, the rate of dividend has been raised by 1 per cent. In this direction, the directors have to proceed gradually. There will be difficult times ahead, and we shall have to meet with keen competition from some, if not all the banks recently floated. The strengthening and consolidation of the Bank's position is our first concern, and we trust the shareholders will appreciate the directors' action in setting apart substantial amounts from the profits of the year to meet the onslaught of lean years" Central Bank of India Ltd. Meeting held in March 1943

2. "I may just remind you that it was only the other day—four years ago in fact—that we were seriously considering the question of curtailing out-put. Boom times do not last. They are usually followed by years of depression and it behoves us to see that we do not dissipate all our earnings of prosperous years without making some provision for the years when profits dwindle down to almost vanishing

point and mills find it hard to provide the finance to renew machinery, to expand plant, to meet all the other expenditure necessary to meet fierce competition in a falling market We, at least, those of us who have no longer remained young, have witnessed the cycle of prosperity and depression once and it would be very unwise if we do not profit from past experience." The Swadeshi Mills Co., Ltd., Bombay—Meeting held in April 1943.

3. "I would now like to turn to the question of finance which, I think you will agree, is, from the Corporation's point of view, of the highest importance. In days gone by, the control of finance in a Corporation such as yours was a matter meriting the constant attention of the directors but under the circumstances which war has brought in its train, the financial control of manufacturing concerns is gradually being assumed with greater and greater force by the Hon'ble Member for Finance in India. The Finance Member was, a few years ago, regarded, on the introduction of the Excess Profits Tax, as the senior, but sleeping, partner of most business concerns in India and, as time goes on, he certainly continues to increase his interest in the disposal of any profits earned as the result of industrial or commercial enterprise; in fact, his share of the profits now has attained such dimensions that there is little incentive left to increase either efficiency or production.

"You must all be aware of the recent Budget proposals which were placed before the Central Legislature by the Finance Member and how these proposals in subtle manner seek to immobilise what the Honourable Member regards as the surplus finance of any business and to limit, if not curtail, the distribution of profits by way of dividends. While perhaps there is justification for the steps, which the Finance Member has felt constrained to take in this connection, it must also be borne in mind that quite apart from the distribution of profits by way of dividends, every manufacturing business in India now increasingly requires working capital to a much greater extent than pre-war owing to the very material rise which has taken place in the cost of almost every element required in manufacture. It is accordingly, becoming more and more expensive to finance manufacturing businesses of the kind in which you, as shareholders of this Corporation, are interested.

"The policy which your directors adopted at the out-break of War in recommending that the dividend on the written down ordinary shares should be maintained at 25% is accordingly very fully justified. I have given you very cogent reasons in the past why the policy adopted by your directors could be regarded as sound and as in your own best interests and last year I stated that I was sure you would recognise that by maintaining instead of increasing the dividend the Corporation was in a small way helping to combat the very serious evil of inflation with which India was then threatened. I can only emphasise those remarks today and also repeat that any increase in the dividend which could have been made would have been at the expense of the Corporation's financial resources which, as I think is very obvious, would distinctly be bad policy and definitely against your interests.

"Reference has been made in the Directors' Report to the compulsory E.P.T. deposit which the Corporation has nnw to make and to the fact that, to meet this legal liability and alsn tn provide for the estimated liability for taxation, it has been necessary, out of the profits earned in 1943, to set aside the colossal figure of Rs. 165 lakhs. In the past few years, it has been the Directors' aim that, while maintaining the ordinary dividend, any balance nf prnfits shonld be placed to Reserve so that the money would be available within the framework of the Corporation. Although in the year 1942 advantage was taken of the option to deposit by way of investment certain sums under the E.P.T. Act, that option has now been withdrawn and the Corporation is compelled to allocate a considerable sum of money as a compnlsory E.P.T. deposit. It is true that these sums will be refnnded after the war with interest at 2%, and it is hoped with an additional contribution from Government, thus providing the wherewithal to enable the process of rehabilitation to be carried on. For that reason, as explained in the Directors Report, your directors do not feel that it is now necessary to make further provision for Rehabilitation and Obsolescence nor In fact could any snch provision have been made if the normal ordinary dividend Is to be continued and I am snre that it is your unanimous wish that this shonld be the case.

"It was stated In the Press not long ago that, the Finance Member's recent proposals will leave companies only with their 'standard profits' less the amount of Income and snper taxes thereon. That statement however does not allow for snch accretion tn the original standard profit as Is permissible under the E. P. T. Act on account of the increased working capital employed in a bnsiness The shareholders will therefore recognise that the Corporation and they have gained materially by the policy which has been adopted by the Board In the past in recommending that the dividend should not be increased. The money thus retained In the business has increased the amount of working capital and, as a conseqnence, has angmented the amount of standard profit which is free from Excess Profits Taxation. Undoubtedly, however, the virtual freezing of liqnid cash balances, which the Finance Member's Budget proposals involve, will have serious conseqnences on the financing of indnstrial enterprise in India. By their stewardship In the past few years, however, your directors snbmit that the consequences on this Corporation will not be so burdensome as on those companies who have imprndently dissipated their profits by way of larger dividends and are now faced with the necessity of reducing the return to shareholders in the shape of dividend or, alternatively, of dissipating still further their financial resources beyond reasonable limits.

"While on the snbject nf Taxatinn, it may be of interest to you to know that in order to comply with its recent legal liability to taxation the Corporation has had to provide during the war years over Rs. 3¼ crores and can therefore be said tn have made a very material contribution to the cost of winning the War.

"I can now only assnre you that ynnr directors will do everything within their power to maintain the nrdinary dividend at 4 annas per share in futnre and, provided the Hon'ble Member for Finance does not at a later date introduce even greater measnres of restriction, I sincerely trust that it will be possible for the Board to do so.

"On a previous occasion I took the opportunity of pointing out to the holders of ordinary shares in the Corporation that, despite the lean years which bad been encountered by the Corporation in the past, the return which they had received on their shares since the inception of the Corporation give them an income which was equal to, and even better than, that which would have been available to them, had the money been invested in Trust Securities. I am happy on this occasion to say that, with each year, the position in this regard improves and it is a matter of some satisfaction, I am sure, to those shareholders who have loyally held their ordinary shares since 1920 that, if they so desired, they would now be able to sell these written down shares in the open market at a price which taking into consideration the extent of capital previously refunded would enable them to close the account without loss to themselves. "The British India Corporation, Ltd.—Annual meeting held on 25th March 1944.

4. "Compared to the dividends declared for the two previous periods (56% and 40%), perhaps I may owe you an explanation why we recommend a dividend of only 24 per cent. But anyone who analyses our report will easily understand that, in view of the new rates of taxes and provisions to make E.P.T. compulsory deposits, it is not a sound policy to declare dividends higher than the situation really warrants. We must appreciate the policy of the Government of India and its magnificent efforts by way of anti-inflationary measures. In my view this, a dividend of 24 per cent. must be considered very satisfactory. It is a matter for regret that as soon as it was known that the Board recommended 24 per cent., a firm of share brokers characterised the dividend as disappointing. However another firm of share brokers came out with a report that the balance sheet of our mills revealed a strong position.

"In my view, taking all factors into consideration, this dividend should not be considered either as disappointing or low. It may, perhaps, be possible to encroach upon the reserve funds already accumulated and declare spectacular dividends. But it is my considered view that the adoption of such a course cannot be considered to be in the interests of the mills. I am aware of the circumstances that after the announcement of the dividend, the market price of our shares came down. It is unfortunate that prices should be made to *depend upon the dividends declared*. Even at the present level of prices, the dividend earned works out at the rate of more than 5 per cent.

"I wish sincerely that investors should study the working of the mills, its results, the capacity of the managing agents, and its future prospects, and form sound conclusions while assessing the worth and the value of any industrial concern and its shares, and remember that the declaration of high dividends is not necessarily an index of the strength of the concern.

'It will be gratifying to note that already we had deposited with the Government Rs. 8,05,339 as excess profits tax refund deposit. We have set apart a sum of Rs. 13,40,000 and odd as general reserve from which E.P.T. compulsory deposit will be paid and when these deposits are returned by the Government together with a proportionate share, the mills will be in the fortunate position of enjoying a grand

reserve which will enable the mills to face the post-war period and the future with confidence.

"It may not also be fair to compare the dividend which has now been recommended for our mills with the dividend declared by a majority of the mills situated in Coimbatore, because it has to be noted while those mills closed their financial year by 31st December, 1943, our mills closed its accounts by 31st March 1944 The E.P.T. deposit, which was optional till April 1943 was made compulsory thereafter; and so we had to deposit with the Government the said Rs. 8,05,339. Again notice must be taken of the increase in the proportion of the deposit of the E.P.T. made after 31st March 1944. If conditions in respect of taxation and deposits remained as before, it might have been possible to recommend a very high dividend. But we need not at all regret the circumstances in which we are obliged to recommend the dividend at 24 per cent. for the resaons I have already referred to in extenso. "The Lakshmi Mills Co, Ltd., Annual meeting held on 9th July 1944.

5. "In disposing of the profits made by the Company in the last three and a half years, your directors have been guided by two main considerations. First, the imperative need for conserving the company's resources and strengthening its finances so as to enable us to face the future with confidence. We would have to be prepared for a possible postwar trade slump, though one may hope that such a reverse might be averted or, if inevitable, might not be of long duration. At the same time, the need for revitalising and remodernising the Mills' plant and machinery, which are over twenty years old and have been subjected to undue stress and strain in the past few years, is very urgent. All this needs plenty of finance and the reserves of nearly Rs. 19 lakhs which we have now built up should stand us in good stead in meeting this demand.

"Secondly, your directors have attempted to the best of their ability to cooperate with the Government in their anti-inflationary measures by resisting the temptation of high dividends out of what may, generally speaking, be called war time prosperity and by retaining the bulk of our earnings in and for the benefit of the industry itself. Thus, out of a total profit of 67 lakhs made during the past three and a half years, as much as Rs 42 lakhs or 62 per cent have been retained in the industry itself. This has enabled the Company not only to become free from all external indebtedness but has also added substantially to its fluid resources" Sri Krishnarajendra Mills, Ltd., Mysore—Annual meeting held on 14th October 1944.

## CHAPTER 6.

### THE CHAIRMAN'S SPEECH.

The Balance Sheet, the Profit & Loss Account and the Directors' Report, which have been discussed in the preceding pages, are all required to be published by law. They are usually printed together and are known as the 'published accounts'. At the ordinary general meeting of a company it is the usual practice for the chairman to make a speech in placing the audited accounts and the directors' report before the members for their consideration and approval. It is not legally necessary that the chairman's should do so, but this is always done. A printed copy of the chairman's speech is usually made available for the information of those interested in the company. In recent years many companies have adopted the practice of publishing their chairmen's statement or review simultaneously with the annual accounts, a procedure that has a clear advantage for the shareholders, since many of them do not attend the ordinary general meeting. The chairman's speech or statement or review serves to supplement and elucidate the information contained in the accounts.

The function and contents of a chairman's speech are very well described in the following article which appeared in the *Economist* dated 25th December 1937 :—

"Approximately five thousand British public companies invite their shareholders, once every year, to a *folk-moot*. If half the proprietors of even a moderate-sized company attended, the chairman would have a larger audience than Signor Mussolini ever addressed from the Palazzo Venezia. No hall in England could possibly contain the 150,000 ordinary shareholders of Imperial Chemical Industries. But no secretary ever lost sleep on that account; for shareholders simply do not come trooping by battalions. Contrary to all theatrical canons, the best shows draw the thinnest houses. Only a passed dividend, a heavy loss or a reconstruction scheme can really pack the hall; a crowded meeting is usually an angry meeting. Shareholders who cannot attend, however, are given special facilities for voting in favour of the chairman's policy before they have heard his speech.

The meeting opens with the reading of accounts which are always taken as read. Discussion of greivances precedes the voting of supply—by shareholders to themselves. Many crowded hours of criticism, interruption and cross-questioning have gone down to history in a single sentence: "After some discussion—the accounts were adopted." The main resolution is ultimately put, defeated (if it be very controversial) by those present, and duly carried by the absent shareholders. The meeting ends with a directorial election in the Russian manner. Candidates and vacancies are identical. Everybody is successful, and everybody has served before.

"Despite these anomalies, however, the company meeting system has worked with a minimum of friction and (except in a small minority of instances) to the reasonable satisfaction of the majority of investors for a good many years. Ninety-nine per cent. of company meetings are merely formal: for shareholders are wisely content to leave their interests in the capable hands of those whose prime duty is to direct and manage them. But they do afford chairmen an opportunity to establish direct personal touch with a scattered army of beneficial proprietors whom they may never meet in the flesh.

'Who is the perfect chairman? What is he that every junior director would wish to be? There are manuals of "dos and don'ts" on many subjects from golf to writing for the Press; but no one has yet compiled a list of the topics which conscientious company chairmen ought to discuss, and those they should wisely avoid. We may perhaps be permitted to make a few tentative suggestions, based in good faith on the discipline of many years' attendance at company meetings. Doubtless progressive earnings and dividends, maintained or increased over many years, speak louder to shareholders than any number of words. But the real audience which the chairman of even a small company addresses is far wider even than the total of the proprietors, since it includes all investors, large or small, who may choose to become proprietors in the future. Such an audience will pardon, and even welcome, the enthusiastic satisfaction of a directorial board with its own achievements. Conversely, it will be sympathetic, in time of depression, to a frank avowal of difficulties encountered. It does not expect chairmen to give their companies a bad advertisement or to do the shareholders' job of criticism for them. *What it desires, above all things, is news about a company, its achievements, its aims, its hopes and its problems.*

'Investors, indeed, have an insatiable appetite for positive facts, from which they can draw their own conclusions with the assurance that no consideration which is basic to their decision has been omitted. The best speech can never be a satisfactory substitute for detailed and informative annual accounts. Its ultimate function, indeed, is to give these annual figures their due perspective, to remove misapprehensions, to put present results into relationship with the past and the future, and to elucidate the causes which have brought them about There is obvious utility in a speech which specifies the directions in which a company's business is expanding, the new products it is manufacturing and the new branches it is about to open. Equally useful is the speech which describes the background of the industry in which the company is a single unit.

"Whether an address which amply covers all these points can leave any room for controversial propaganda is perhaps an open question. A certain seeing of facts through rose-coloured spectacles, again, may be permissible, if shareholders and investors can determine the tint employed more or less accurately. The rostrum is not a judicial bench, and he is a poor father who does not praise his own child. But investors may rightly ask that what is misleading or irrelevent or sufficiently condensed and partial to be both, shall be excluded. On the whole, they have reason to complain of speeches which tell them too little rather than too much. From their viewpoint, the least useful address is the one, which studiously avoids every unfavourable possi-

bility. And the most dangerons is the speech (happily rare to-day) made with one eye on the price of a company's shares on the Stock Exchange.

"For the rest, the best speeches will always express some indefinable *trait* of the speaker's personality. When ought they to be made? An increasing number of higbly sncecssful businesses is following the practice of including the text of the chairman's speech in the annual report to its shareholders. This device car never be a complete subsitute for present methods of giving wide publicity to company speeches; for a chairman's effective andience inclndes potential as well as actual shareholders, who may be synonymons with the whole body of contemporary investors There can be nothing but commendation, however, for every innovation which tends to stimulate the interest of shareholders in their companies, to bring them in greater numbers to annual meetings and to increase the number and pertinence of the questions they put. The problem of overcoming the apathy of shareholders over the affairs of their own companies—a corollary of the widening diffusion of capital ownership—can only be solved eventually by the investor himself. But chairmen aod directors can make a valuable contribution by encouraging every development calcnlated to impair their own peace and qniet."

**Publication of Chairmen's Speeches.** Why wide publicity should be given to chairmen's speeches delivered at company meetings is fully explained in the following paragraphs taken from the *Indian Finance* dated 25th January 1941 :—

Two of the important leading industries in India have had occasion to bring to public attention their position and prospects; and, when a general review of Indian industry is beset with so many difficulties, the coincidence is to be welcomed In fact, there are always two ways of appraising economic conditions There is the method of the ultra-academic economist, who deals, in the main, not with economic facts in the raw, but only in the form in which they emerge from the statistical laboratory. He prefers index numbers to prices, graphs to tables, bulletins and returns of associations or departments of government to the reports of particnlar companies. He would, no doubt, recognise the need for verifying his conclusions by reference to actual conditions, but he would not think of looking into the reports of companies to make a picture of the indostry or of putting the pictures of each and every indostry togetber to make np the composite picture of Indostry as a whole. It is the financial journalist who favours the inductive method. His impressions are formed by the daily study of the miniutiæ of the markets Market reports, reports of joint stock companies, trade returns, official and organisational bulletins—all these have to be studied in detail from day to day. The impressions are clear, thougb the mental pictures so formed are necessarily diminutive and their bearings on the rest of the panorama of economic life are not always obvious. But Walt Disney makes his full length features; and the effect is even more impressive tban that of the snper-productions from the usoal studios.

The Cbairman's speech at the annnal meeting of a leading company has thus a special value. It is a picture of the industry drawn by those who have a stake in it and who are in touch with it, day in and

day out. It is not a learned deduction from statistical abstractions, from facts obtained secondhand. It is a presentation promoted by self-interest, but bridled at the same time by the knowledge that, where questions of public interest are involved, there are governmental authorities and publicists and even their own competitors to question inaccurate statements or inequitable claims. When a Chairman speaks at the annual meeting, he is addressing not the shareholders alone, most of whom nominate the Chairman or his immediate associates as their proxy, but the country as a whole. The speech calls for and fully deserves the utmost publicity To smother it within the four walls of the Company's Registered office is to deprive it of all its importance and usefulness, alike to the company and to the public. And yet it is more than *Indian Finance* has been able to do to induce the leading companies in India to give the best publicity to their Chairman's speeches. I cannot believe that expenses are the primary consideration. For the question does not arise except in the case of institutions which are in a position to make the outlay and reap a return. It is rather a question of certain inhibitory modes of thought which incapacitate people for a proper appreciation of the value of such publicity. Even in the case of the two speeches which form the theme for this week's Gossip, the Associated Cement Companies, Ltd. has, during this year chosen to restrict the publicity afforded to its Chairman's speech. In the previous one year or two, space was taken for the publication of the speech ; and as if the Company has had too much of a good thing, the policy has been reversed. In the case of the Bengal Coal Company. I do not know why Managing Agents in India are so chary of introducing in India customs and practices which are accepted as salutary in other countries. How can the publication of a Chairman's speech in journals of standing be supposed to be conditioned by the vicissitudes of business activity or by the varying need of public support ? Have not the cement and the coal industries the same obligations as others to maintain a healthy public opinion on economic questions ? And even if one were to look at it from a narrower standpoint, is not the investor, the shareholder, entitled to have these speeches in the pages of the journal on which he relies for all the information he needs about companies and markets ? A journal which has specialised in catering to the needs of investors all over India has a special claim on the appropriations of joint stock companies for publicity, whether of the statutory or of the optional kind. But what is more important the readers of the journal who are, in fact, the shareholders of their companies are entitled to have all the matter pertaining to these companies brought home to them through the columns of this journal. And yet, it is as patronage that most people insist on looking at the request for publication of company notices or Chairman's speeches. The change is being achieved, no doubt, but the pace is often disheartening. And a reverse on one side naturally enhances the value of progress in another.

The following is a fine specimen of a Chairman's speech :—

CAWNPORE

25th March 1944.

### THE BRITISH INDIA CORPORATION, LIMITED

The twentyfourth Annual General Meeting of The British India Corporation, Limited, took place in Cawnpore to day. Sir Robert

Menzies, chairman of Directors, who presided at the Meeting addressed the Shareholders as follows :—

Perhaps I need hardly remind you that this, the Twentyfourth Annual General Meeting of the Shareholders of the Corporation, is also the fifth Annual General Meeting to assemble during the present War. The Balance Sheet which is to be considered today has, accordingly, been produced under conditions far removed from normal and many of the figures contained in the Balance Sheet and accounts now before you are, similarly, abnormal and cannot therefore bear any strict comparison, even with some of the War years, far less the years immediately pre-war. As I said at this time last year, ordinary manufacturing and trading operations in Industry are apt completely to be upset by war-time conditions and that remark, which was true of the circumstances which governed the operations of the Branches of your Corporation in 1942, is again equally true of 1943.

You will, I have no doubt, have appreciated, from the figures which have been placed before you in the circulated Balance Sheet and Accounts, that the Branches have continued to give of their best in the War effort. Once more, during the year 1943, over 80 per cent of the goods manufactured by the Corporation were taken up by the Government of India for the Defence Services and we can again therefore regard, with, I think, justifiable pride, the part which the Corporation and its Branches have continued to play in India's War effort, an effort which is anything but mean. Striking although some of the figures which appear in the Balance Sheet may be, even these would have been surpassed had the various commodities required throughout the year always been immediately available. It would be idle to deny that some anxiety has been caused through shortages of certain raw materials which are essential for the Corporation's manufacturing programme; these shortages have been caused, I need hardly assure you, by circumstances in no way within the Corporation's control. It is however only to be expected that manufacturing demands in war-time should very considerably outstrip normal peace-time requirements and that, in the circumstances, certain items essential to the production of the finished article must, from time to time, be in short supply even if of indigenous origin. Even with these disadvantages to contend with, the sales effected by the Corporation during 1943 again broke all records, but I cannot, at the moment, hold out any hope that the current year will, in that respect, surpass its predecessor. We have recently heard from one of His Majesty's Ministers that War production in the United Kingdom,—that veritable hive of War Industry—reached its peak in 1943 and, so far as one is in a position to judge at the moment, these remarks apply equally to your Corporation. The reasons for this state of affairs are not, I think, difficult to determine. I have already explained the difficulties with which the Management has been faced in regard to raw materials and other essentials of manufacture and it is but fair that I should make passing mention that, whilst the devoted staffs of the Corporation continue to give of their best, indications, of what is known in medical circles as "Industrial Fatigue", are already manifesting themselves, though, as yet, not in any marked degree.

The year 1943, which saw the fourth anniversary of the outbreak of War, was a year of Allied progress during which it was aptly remarked that we had reached the end of the beginning and had, in fact, started on the beginning of the end–the end that will lead to a complete Allied Victory. It is no part of my duty to-day to refer in detail to the resounding victories which were achieved by the Allies during 1943 but it was a momentous year, the results of which give us an outlook full of confidence for the future. In so far as the soil of India is concerned, the War has made little practical impression and the heinous, would-be invader has been held at bay and, in fact, has been prevented from launching an attack of any moment whatsoever, even from the Air. For this state of affairs, our grateful thanks are again due to the Allied Defence Services which, since last we met, have assembled in India and on her Eastern Frontiers in impressive numbers and with formidable equipment of the latest type, not only to protect India from invasion but to carry the War more actively into the Enemy's camp. We can, as I have said, regard the future with sober but complete confidence albeit with the knowledge that the more all concerned now concentrate on production for War and the actual training for, and waging of, war, the sooner will we achieve, both in the West and in the East, that Victory for which we all so ardently long.

It is sad indeed to think that the present-day older generation should have become engulfed in the turmoils of two gigantic Wars. Let us, therefore, sincerely hope that when this War is over, we will be finished with War for generations to come. I am sure it is the fervent wish of those who have experienced the last two Wars that the young generation now growing up may be permitted throughout to live a life of peaceful and useful activity, without further disastrous upsets of this nature.

I am happy again to be in a position to make public mention of the Directors' and, I am sure, your, keen appreciation of the manner in which the Labour employed by the Corporation has discharged its duties during the past year. The year which we now review did not witness any major political upheavel in India, as did the previous year, but, nevertheless, we should, I submit, be thankful for another year of marked Labour stability.

I am glad too to record that, so far as the Branches of your Corporation are concerned, the continued expenditure on the provision of Air Raid Precautionary measures for the protection of Labour and Property has,—at least meantime-come to an end. We may be happy that this is so and that the threat of enemy action, so far as the Corporation is directly concerned, has, in the opinion of the Authorities, been effectively challenged and disposed of.

Last year I mentioned that the question of coal supplies had been, in 1942, a matter of considerable concern to the Management. Coal again formed a major problem for the Management during 1943 and I regret to say that there were several instances where Branches of the Corporation had to close down owing to lack of fuel. In this, of course, the Corporation was not alone and you perhaps already appreciate the anxiety which has been caused throughout the length and breadth of India by the difficulties of placing coal just where it is wanted at the

proper time. In the Coal Fields an acute shortage of labour, brought about by unusual and depressing circumstances, was, during a portion of the year, responsible for a material drop in raisings and you will have read in the Press of the steps which have been taken by the Mine Owners and by the Government of India alike to encourage Labour to return to the Mines. I am glad to say that these efforts have apparently met with some measure of success and that raisings are now reported to be more satisfactory. The difficulties, however, which have been encountered have not only arisen from the unavailability of coal but once more, the main difficulty comes from the lack of transportation. As time goes on and as the War drags on, the load which has been placed upon the Transportation System in India becomes heavier and heavier, with consequent increased wear and tear upon engines and rolling stock. We are assured however that the Government of India and the Railway Board are doing everything humanly possible to maintain and, in fact, to increase railway facilities but, notwithstanding all these efforts, the shortage of railway wagons against urgent requirements continues and, while one cannot but admire the efforts which have been made by Officials of the Railways generally, I regret that I cannot feel that those Administrations have received the whole-hearted support, which they might have expected, from railway subordinate staffs. It is an open secret that certain of the latter grade of railway employee have regarded the War as a Heaven-sent means of illicit personal enrichment, an evil which it is apparently impossible to eradicate and even most difficult to detect or to arrest. We are, however, assured that all possible steps are being taken and we can only hope that conditions will improve and will not further deteriorate.

So far as coal supplies to your Branch at Dhariwal, in the Punjab, are concerned, it was necessary to depend upon such direct sendings as were possible and it is a matter of regret that, apart from an insufficiency in quantity, the quality of the coal supplied was most inferior and had a marked effect upon production. On several occasions that Branch had to close down completely and I regret to add that it is once again closed down owing to lack of fuel. In Cawnpore, Industry was supplied under pooling arrangements organized by the Employer's Association of Northern India in collaboration with the District Magistrate, the Supply Department and the Railway Authorities. These arrangements provided a solution of at least some of the difficulties previously encountered and they continue to operate although, here again, the quality of coal supplied has been, in many instances, very inferior. The fact remains, however, that during the latter part of 1943, few local Industries were completely bereft of coal at any time. This state of affairs, of course, can partly be ascribed to the immense havoc wrought by the elements to railway communications on the other side of the main Coal Fields of India which calamity enabled supplies, normally intended for elsewhere, to be despatched upcountry. I cannot think that we are yet out of the wood in regard to coal supplies and can only hope that we will be able to carry on, even from hand to mouth, in future.

Reverting now to the subject of Labour, your Corporation, in common with other Employers, arranged throughout the year to make available to all workers food grains at rates which, as stated in the Directors' Report, were generally less than the Government controlled

rates. This boon has, it is understood, been suitably appreciated by Labour. The cost of living index figure showed a very distinct upward tendency throughout most of the year but towards the end of 1943, as the result of the introduction of Government control in certain directions and also, directly, as a result of the sale of food grains at cheap prices to workers, the cost of living index figure, as applied to Industrial Labour in Cawnpore, showed a downward tendency thus assisting the Government of India in their drive against the evil of inflation to which I made reference last year. The Loud Speaker Systems in the Corporation's Mills and Factories, to which I also referred last year, have continued to be utilized throughout the past year and again this amenity has been much appreciated by the workers. You have been informed in the Directors' Report that provision has been made for a bonus payment to workers. This bonus has now been distributed by the various Branches of the Corporation and was paid at rates similar to those which applied to the year 1942. (In this connection, it is significant that while the Government of India in the Department of Finance seeks, as a part of the anti-inflationary drive, to limit such payments as War Dear Food Allowance and Bonus, the Government of India in the Department of Labour apparently seeks to enhance these payments, thus placing Employers in a most difficult position.) The Department of Labour of the Central Government is taking energetic action to improve the social security of labour throughout India and a spate of Labour Legislation is now on the anvil. At the Tripartite Labour Conference, held in New Delhi last September, it was recommended that, with a view to providing adequate materials on which to plan a policy of social security for Labour, the Central Government, in co-operation with the Government of Provinces of British India, Indian States and the Chamber of Princes, should immediately set up machinery to investigate questions of wages and earnings, employment and housing and social conditions generally and that, as soon as possible after receipt of the required statistics and other data, the Central Government should appoint a mixed Committee to formulate plans of social security. Certain Investigating Committees have already, as a result of this recommendation, been appointed by the Central Government. Other subjects, having as their aim, the improvement of amenities for Labour, which are receiving active attention from the Central Government, include Sickness Insurance Benefits, Compensation for involuntary unemployment due to shortage of coal, raw materials, etc., Minimum Wages, Wage Control, greater Labour representation in the Legislatures Provision of Standing Orders in Factories for all operatives, the introduction of Provident Funds for workers, the laying down of principles for fixing Dear Food Allowances, the setting up of Labour Exchanges, investigation of the causes of absenteeism, the setting up of Tripartite organizations in the Provinces and the provision of Canteens for workers. In this last connection, I was recently misreported in the Press as having said that Employers were opposed to the organization of Canteens on the grounds that such amenities might be looked at with suspicion as profit making devices What I actually said, on the occasion in question, was that I felt sure that most Employers would be sympathetically inclined to the introduction of Canteens wherever possible, but I asked my audience to remember that there were several inherent difficulties in the way, including, in certain instances, lack of suitable accommodation, the impossibility of catering, with acceptance, for all castes and religions, the difficulty of employing Contractors to

run Canteens as no Contractor would be prepared to undertake this work without a profit motive and the thought that, if the Canteens were run by the Employers themselves, it might be imputed to them that they were doing so also with a similar motive.

When one thinks of the welter or Labour legislation which I have recently mentioned, it would seem that the almost complete absence of reliable statistical data will act as a brake on Government's intentions but as I have indicated, steps are now being taken to collect specific data in certain directions and it is to be noted that, in almost every direction, in which the Central Government seeks to improve the lot of Labour, there appears to be a determined policy on the part of Government to avoid any share of the financial liability which is inevitably attached to these schemes and it seems that the entire expense of any such enactments will fall upon the Employer.

During the past year many distinguished visitors have visited the Workmen's Settlements maintained by the Corporation and were obviously impressed by the extent of the Welfare amenities therein provided.

I have already made brief reference to the subject of Government control arising from the Hoarding and Profiteering Prevention Ordinance which was promulgated in October 1943. Controls, which have been introduced and which affect the interests of the shareholders of this Corporation, concern Cotton and Woollen Manufactures. You are probably aware that, in the middle of 1943, a Cotton Textiles Control Board, of which my colleague, Mr. John Tinker, is a Member, was, set up by the Government of India and that useful action has already been taken by this Board to reduce gradually the selling prices at which manufactured cotton materials may be sold. There is no gainsaying the fact that prior to the establishment of this Control Board, the prices obtainable for cotton textile goods were, to put it bluntly, fantastic and I can, I think, honestly say that no Manufacturer of repute in India considered that he was justified in accepting these rates other than as an Agent of Government so that the lion's share of the profits thus accruing would revert to the coffers of Government in the shape of Excess Profits Tax. It was perhaps somewhat anomalous that manufacturers should find themselves thus pitchforked into the role of Tax Collectors for Government.

Later in the year, the Government of India announced that steps were being taken to curtail the demands of the Defence Services for woollen manufactures and it might here be noted that, ever since the outbreak of War, the total production of the entire Woollen Industry in India has been taken up by the Department of Supply against War requirements. Under the Woollen Textiles Control Order which was issued last month, a certain proportion of the production of the woollen Industry in India will be diverted from the Defence Services to Civilian Market, distributing and selling arrangements remaining in the hands of the Government of India A Woollen Textiles Control Committee has also been established of which Committee another of my colleagues, Mr. W R. Watt, is Chairman. Here again, commendable efforts are being made to control prices on a reasonable level but the success of this Order will depend very largely on the conscience of the purchasing public inasmuch as the comparatively small quantity

of woollen materials which will thus be freed for civilian purchase, would not justify the introduction of any India-wide rationing system for these goods

In regard to the question of Government Control generally, while the aim of Government is perfectly clear, the fact remains that in certain directions, owing to the lack of suitable Inspecting Staffs, that aim has not been attained and, in fact, the very reverse has been the case in as much as black markets have undoubtedly been created. It seems a very patent fact that it is useless for the Central Government to introduce measures of control unless they have provided the necessary Inspectorate Staff to ensure compliance with these orders. No reasonable man would desire to see inflation gain a greater hold on India than was the case in 1943 and it is to be hoped that motives of personal gain — in other words, profiteering — will come to be regarded as anti-social acts to a greater degree in future than is at present the case.

It will have been obvious to you that to maintain production to the scale required, there must have been heavy wear and tear on the Corporation's Plant. I have already, in past years, made reference to the difficulty of keeping the Corporation's Plant at the pitch of perfection which your Directors would wish but you may rest assured that everything possible, that present day circumstances will permit, is being done to maintain that plant in as efficient a state as possible. It is obvious, however that, when the War is over and new plant once more becomes available, a heavy programme of replacement lies before the Corporation.

During the past year, the sum of Rs. 9 lakhs has been allowed by way of Depreciation and it must be a matter for satisfaction to you that notwithstanding additions to Block during the year of approximately Rs. 5 lakhs, the total Block now stands at the very conservative figure of under Rs. 56 lakhs. In this connection, it is interesting to note that, in the last four War years, the sales effected by the Corporation have totalled nearly Rs. 32 Crores and it may be assumed that of these sales, at least Rs 25 Crores have been against orders placed by the Government of India for War purposes.

I would now like to turn to the question of Finance which, I think, you will agree, is, from the Corporation's point of view, of the highest importance. In days gone by, the control of Finance in a Corporation such as yours was a matter meriting the constant attention of the Directors but, under the circumstances which War has brought in its train, the financial control of manufacturing concerns is gradually being assumed with greater and greater force by the Hon'ble Member for Finance in India The Finance Member was, a few years ago, regarded on the introduction of the Excess Profits Tax, as the senior, but sleeping, partner of most business concerns in India and, as time goes on, he certainly continues to increase his interest in the disposal of any profits earned as the result of industrial or commercial enterprise; in fact, his share of the profits now has attained such dimensions that there is little incentive left to increase either efficiency or production. You must all be aware of the recent Budget proposals which were placed before the Central Legislature by the Finance Member and how these proposals, in subtle manner, seek to immobilise what the Honourable Member regards as the surplus finance of any business and to limit, if not curtail, the distribution of profits by way of dividends. While perhaps there is justification for the steps which the Finance Member

has felt constrained to take in this connection, it must also be borne in mind that quite apart from the distribution of profits by way of dividends, every manufacturing business in India now increasingly requires working Capital to a much greater extent than pre war owing to the very material rise which has taken place in the cost of almost every elment required in manufacture. It is, accordingly, becoming more and more expensive to finance manufacturing businesses of the kind in which you, as shareholders of this Corporation, are interested.

The policy which your Directors adopted at the outbreak of War in recommending that the dividend on the written down Ordinary Shares should be maintained at 25 per cent is accordingly very fully jostified. I have given you very cogent reasons in the past why the policy adopted by your Directors could he regarded as sound and as in your own best interests and, last year, I stated that I was sure yon would recognise that by maintaining, instead of increasing, the dividend, the Corporation was in a small way helping to combat the very serious evil of inflation with which India was then threatened. I can only emphasize these remarks today and also repeat that any increase in the dividend which could have been made would have been at the expense of the Corporation's financial resources which, as I think is very obvious, would, distinctly, be bad policy and definitely against your interests.

Reference has been made in the Directors' Report to the compulsory E. P. T. deposit which the Corporation has now to make and to the fact that, to meet this legal liability, and also to provide for the estimated liability for taxation, it has been necessary, out of the profits earned in 1943, to set aside the colossal figure of Rs 165 lakhs. In the past few years, it has been the Directors' aim that, while maintaining the Ordinary dividend, any balance of profits should he placed to Reserve so that the money would he available within the framework of the Corporation. Although, in the year 1942, advantage was taken of the option to deposit, by way of investment, certain sums under the E P. T. Act, that option has now been withdrawn and the Corporation is compelled to allocate a considerable sum of money as a compulsory E. P. T. deposit. It is true that these sums will be refunded after the War with interest at 2 per cent and, it is hoped, with an additional 50 per cent contribution from Government, thus providing the wherewithal to enable the process of rehabilitation to be carried on. For that reason, as explained in the Directors' Report, your Directors do not feel that it is now necessary to make further provision for Rehabilitation and Obsolescence nor, in fact, could any such provision have been made if the normal Ordinary dividend is to be continued and I am sure that it is your unanimous wish that this should be the case.

It was stated in the Press not long ago that the Finance Member's recent proposals will leave Companies only with their 'Standard Profits'' less the amount of Income and Super Taxes thereon. That statement, however, does not allow for such accretion to the original Standard Profit as is permissible under the E. P. T Act on account of the increasing Capital employed in a business. The shareholders will therefore recognise that the Corporation, and they, have gained materially by the policy which has been adopted by the Board in the past in recommending that the dividend should not be increased. The money thus retained in the business has increased the amount of working capital and, as a consequence, has augmented the amount of Standard

Profit which is free from Excess Profits Taxation. Undoubtedly, however, the virtual freezing of liquid cash balances, which the Finance Member's Budget proposals involve, will have serious consequences on the financing of industrial enterprise in India. By their stewardship in the past few years, however, your Directors submit that the consequences on this Corporation will not be so burdensome as on those Companies who have imprudently dissipated their profits by way of larger dividends and are now faced with the necessity of reducing the return to shareholders in the shape of dividend, or, alternatively, of dissipating still further their financial resources beyond reasonable limits.

While on the subject of Taxation it may be of interest to you to know that, in order to comply with its recent legal liability to taxation, the Corporation has had to provide, during the war years, over Rs. 3¼ Crores and can therefore be said to have made a very material contribution to the cost of winning the War.

I can now only assure you that your Directors will do everything within their power to maintain the Ordinary dividend at 4 annas per Share in future and, provided the Hono'ble Member for Finance does not, at a later date, introduce even greater measures of restriction, I sincerely trust that it will be possible for the Board to do so.

On a previous occasion I took the opportunity of pointing out to the holders of Ordinary Shares in the Corporation that, despite the lean years which had been encountered by the Corporation in the past, the return which they had received on their Shares since the inception of the Corporation gave them an income which was equal to, and even better than, that which would have been available to them had the money been invested in Trust Securities. I am happy on this occasion to say that, with each year, the position in this regard improves and it is a matter of some satisfaction, I am sure, to those shareholders who have loyally held their Ordinary Shares since 1920 that, if they so desired, they would now be able to sell these written down Shares in the open market at a price which taking into consideration the extent of Capital previously refunded, would enable them to close the account without loss to themselves

My references, so far, to the Accounts now before the Meeting have been in general terms and, as I have already explained, in these abnormal times, comparative comment is virtually out of the question. I therefore do not propose on this occasion to make specific comparisons with previous years and will only refer to the more salient points in the Accounts upon which I have not already touched. It is satisfactory to know that the Corporation's Reserves are gradually being built up and, after being comparatively negligible a few years ago, are now assuming material dimensions. These remarks, of course, do not apply to the Taxation Reserve which is a legal liability.

In regard to the Provident Fund your Directors have been considering during the past year whether it would be desirable to convert the Provident Fund into an Irrevocable Trust Fund so that the benefits, under the Income Tax Act, which accrue to Irrevocable Funds might be realized for the benefit of the Members. A referendum to the staff indicated that a large majority of the Members of the Provident Fund would desire such a change and the Board has so resolved though it is to be noted that the immediate advantages are perhaps more psychological than real, particularly as, when the Fund is converted the rate of

Interest which will be available on Trust Secnrities, less the costs of management, will give a lesser retnrn than is now provided for by the Corporation's articles of Associatinn. The course of conversion is however a slow business though it is hoped that, when the next Balance Sheet appears, the Provident Fund fignres will stand very much reduced by the lifting out of the amonnts pertaining to those members of the staff who favour conversion. The Board have agreed that, in respect of the Members who are against conversion, they shoold be permitted to enjoy the present Fund maintained by the Corporation to which, however, it is not intended to permit further entrance.

It will have been observed that the value of the Stock-in-Trade maintained by the Corporation continnes to increase. The figures now disclosed bear ont my previons remarks in regard to the increased cost of financing the Corporation's bnsiness. Book Debts, always a matter of interest to the shareholders, stand cnnsiderably increased this year but the amount shown in the Balance Sheet of over Rs. 70 lakhs represents almost wholly the amount owing by the Government of India and can, accordingly, be regarded as good, though nnsecured. The Advances for Goods this year are very materially reduced owing to the fact that demands for money to finance the shipment of raw materials from overseas came later in the season than was the case last year. A new item, to which I have already referred, appears on the Assets side of the Balance Sheet under the heading of "Excess Profits Tax Deposit" This amount nf over Rs. 17 lakhs represents the optional deposits previously mentioned. Another indication that it is costing more to finance the Corporation's business under existing circumstances is to be found in the fact that whereas last year there appeared a credit item in the Profit & Loss Acconnt of "Income from Investments less Interest paid ', this year the relative eotry is reversed and appears, as a debit, under the heading "Interest paid less Income from Investments." The figures in the last two Balance Sheets indicate that Interest charges in 1943 exceeded those paid in respect of 1942 by approximately Rs. 2½ lakhs.

As reqnired by law, the Accounts of the Corporation's Subsidiary Company, G. McKenzie & Co (1919) Ltd., have again been published along with the Corporation's Acconnts. These Acconnts show that this offspring continues to flourish. During the past year, our Subsidiary had practically nothing to sell to the public and the continued success which attends Messrs. McKenzies, on this occasion, comes from the operations nf the Workshops maintained by the Company which have been kept bnsily employed on war work thronghout the past year.

Before I conclude my remarks, ynn will perhaps expect me to say something in regard to the topical question of post war reconstruction. You are, of course, aware that the Central Government and certain Provincial Governments bave already appointed Committees to consider the multifarious questions which will require re-adjustment and settlement after the cessation of hostilities. The Corporation is represented on certain of the Committees which bave been appointed both by the Central Government and by the Government nf the United Provinces and, in regard to the more domestic side of this great problem, I would advise that the Management bave taken all such action as is meantime possible.

In regard to the Corporatinn's Woollen interests, you have already been informed that the manufacture nf goods for the civilian market, if

meantime only in a small way, has recently been resumed. These remarks apply to both the Corporation's Woollen Branches and an extension of this class of manufacture, when the time comes, will not provide an insurmountable difficulty as plans and designs have already been fully considered and, provided the requisite raw materials are then available, there should be no difficulty, when the War is over, in turning over the full manufacturing capacity to civilian requirements. In this regard, I should perhaps add that, it is understood to be Government's policy to remove the present Control of the Woollen Industry immediately this is possible, that is, as soon after the cessation of hostilities as is practicable.

Throughout the War the Cawnpore Cotton Mills have only been required to devote a portion of their manufactures to the requirements of the Central Government and accordingly they have continued simultaneously to turn out the types of goods to which they would apply themselves wholly on the cessation of hostilities. Here, accordingly, the problem is a comparatively simple one.

In regard to the Corporation's Leather & Footwear Manufacturing Branches, here again arrangements were made recently to commence the manufacture, in a small way, of civilian footwear. Unfortunately, however, the demand for the Defence Services meantime precludes the possibility of continuing the manufacture of civilian footwear but plans have been made and types and patterns of footwear have been manufactured and approved so that most of the shade work in this direction has already been done.

You may also rest assured that wherever possible, the raw materials, which will be required for the Corporation's ordinary peacetime manufacturing programme, will be made available as and when these are required and, in this important regard, no insuperable difficulty is meantime anticipated.

The Corporation's Branches are also engaged on the close consideration of the extent to which repairs and renovations must be undertaken when the requisite materials again become available after the war and full details are in the course of collection in regard to the replacement of plant programme which will then have to be pursued. I think I can assure you that the Corporation has already progressed in its post-war reconstruction plans so far as is meantime practicable.

The Directors', and your, cordial thanks are again due to the staff of the Corporation for the loyal and efficient services throughout the past year. Again the hours of work have been long and perhaps tedious and work has been arduous but it has again been cheerfully undertaken whilst the Management have done everything in their power to grant such leave as is possible without unduly interfering with the activities of the Corporation. It will be appreciated however that the extent to which leave can meantime be granted is much less than in normal circumstances and is indeed less than your Directors would have wished. I think it will be your wish also that we should extend from this Meeting our good wishes to those of our employees who are taking a more active part in the conduct of the war and are absent on Active Service. Our sympathies will also go out to those who have had the misfortune to be taken prisoners and remain in enemy hands. We sincerely trust that they will all return safely to their former employment in due course.

## CHAPTER 7.

### REFORM OF PUBLISHED ACCOUNTS

The *essential features* of the pnblished accounts of companies have been discussed in the preceding pages. We now come to certain *desirable features* which according to modern accountancy practice are being gradually introduced in the form nf published accounts These desirable improvements in the form of published accounts are, of course, being taken from the British models. It is, therefore, necessary to understand how the present English practice with regard to published accounts has grown.

The English Companies Act nf 1929 requires every public company to publish a balance sheet and a profit and loss account; but, apart from a few particulars, the contents of these documents are not laid down, these being feft to the directors of a company to decide, and the resnlt is that in many cases the balance sheet published is framed in a way designed to conceal rather than to reveal the trne financiaf position of the company, aod the pnblished prnfit and loss account is nn more than a mere skeletnn approprlation statement. Further the Act contains certain provisions dealing specifically with the accounts of holding companies, but there is nn legal necessity to supply the shareholders of the hofding company with the pnblished accounts of the subsidiaries. The present position is, therefore, very unsatisfactory and hnlding companies can, whilst strictly complying with the requirements of the law, present their acconnts in a form which completely cloaks the true veiw of the financial position of the group of companies.

However, soon after the passing of the Act of 1929, came the crash nf the Rnyal Maif Steam Packet Company in 1931, and this opened the eyes of all concerned regarding the unsatisfactory nature of the form of published accounts. But, as the company faw had been amended only a coople of years previously, it was considered rather hasty to press for further reform in company legislation On the other hand, the question of the form of pnblished accounts was considered to be so important in view of the Royal Mail case, that it could not be lightly passed over without doing something to improve the situation. The following extracts taken from the speeches delivered by eminent persons after the Royal Mail case was decided indicate the importance the public at that time attached tn this question ol the form of published accounts :—

"Think of the economic conception nf capital as distinct from income, and then deliberate npon the sorry figure that is cnt in the light of it by your modern fetish of a 'safe' nr 'sound' balance sheet, which lies in almost every line and yet is apprnved by ynu, because it over-states no assets and understates nn liabilities, while it has valuable premises written down to negligible fignres and reserves hidden in innumerable places, or profits held up and tncked away. 'The trnth, the whole troth

and nothing but the truth' cannot be derived from the modern balance sheet, so vaunted for its prudence; but prudence is just as possible without departing from what a balance sheet ought to be—a faithful record of the employment of the total capital invested in the business, whether as an original outlay or retained profits, from which the true rate of profit on invested capital can be determined. Has the shareholder who wishes to sell his holding no rights as to some knowledge of the value of what he is selling ?" (The late Lord Stamp's address to a conference of the society of Incorporated Accountants and Auditors in Liverpool).

"In my view the dangers arising from publishing more informative accounts have been overstated and the legitimate claims of shareholders have not received adequate recognition." (Mr. H. L. H. Hill in his presidential address in 1932 to the Institute of Chartered Accountants in England and Wales).

"The modern balance sheet, where it complies with no more than the maximum requirements of the law, is a model of obscurity" (Sir William MacLintock).

An agitation, stirred by speeches on public platforms and writings in the financial press, was started in connection with the reformation of the published accounts, despite the faulty and inadequate provisions of the company law. Through the exertions of the accountancy profession, the requirements of the London Stock Exchange, the adverse comments of the financial press on the old-fashioned type of accounts, and, above all, on account of an awakening in the shareholders themselves, this movement for more informative accounts began to gather momentum ; and the result is that of late quite a large number of English companies do publish their accounts in a more modern form—a form that can be readily understood by the layman and that will facilitate the reading of the financial position of the concern almost at a glance.

In June 1943, the President of the Board of Trade in the United Kingdom appointed a Committee under the chairmanship of Mr. Justice Cohen to consider and report what major changes were desirable in the English Companies Act of 1929. In June 1945, the Committee submitted its report in which it has made a number of suggestions for the improvement of the published accounts of companies.

In our own country the case is quite different. What is being done in England without legal compulsion but only through the force of public opinion is achieved here under the requirements of company law. The Indian Companies Act of 1913 ( as completely overhauled in 1936 ) prescribes not only the form of the balance sheet but also lays down the contents of the profit and loss accounts ; and it also prescribes the information concerning subsidiary companies which the shareholders of the holding companies are to receive.

The legal requirements with regard to the information to be disclosed in the published accounts are fairly satisfactory ; yet the following are some of the voluntary improvements that are being gradually introduced in the published accounts of certain companies :-

1. **Use of Schedules.** The prescribed form of balance sheet permits the use of schedules which are to be attached to and to form part of the balance sheet. The segregation of details relating to certain

assets and liabilities to separate schedules makes the balance sheet concise. In the absence of schedules the Balance sheet may run to several pages; and nothing is more annoying when attempting an appreciation of the position disclosed by a balance sheet than to keep on turning backwards and forwards.

2. **Inclusion of Comparative Figures.** The figures of the previous year (somtimes printed in red) are included for the purpose of comparison. This is of the greatest importance in examining the progress of the company. An interesting accounting point arises, however, when the comparative figures shown in the latest accounts do not agree in detail with the figures disclosed in the certified figures of the preceding year. This will happen where the figures of the previous year have been adjusted to provide true comparison owing to a reclassification of certain expense charges.

3. **Omission of Annas and Pies.** A further aid to conciseness in published accounts is to dispense with annas and pies, the inclusion of which gives only a misleading impression of accuracy which cannot possibly exist when so many things in the published accounts are mere estimates. The omission of annas and pies is a definite improvement for the reason that it concentrates the attention of the reader on to the 'meat' of the situation. This is specially true where comparative figures are furnished.

The omission of annas and pies is done in two ways :— (*a*) The annas and pies for each individual total are ignored, (*b*) The individual totals are taken to the nearest rupee. In either case, an entry "adjustment due to omission of annas and pies" appear in the balance sheet.

4. **Inclusion of Sterling Figures.** Certain companies having a large number of British shareholders include in their published accounts the sterling equivalents of the individual rupee totals. The sterling figures are worked out at a named rate of exchange (usually 1/6) and are intended for the information of the British shareholders.

5. **Inclusion of Proposed Dividends, etc.** Provision is made in the published accounts for the dividend and reserve appropriations recommended by the directors. Where this is done, the reader of the balance sheet can see at once what effect the directors' proposals will have upon the company's financial position.

6. **Amplification of Directors' Report.** The directors' report is expanded into a careful review of the accounts with explanations for all the principal fluctuations in the various items. Sometimes a separate note on accounts is furnished to the shareholders, and sometimes a note like the following (printed in red) is attached to the published accounts:

"If any shareholder desires to have any information in connection with the Accounts, it is suggested that he writes to the Agents or calls at least two days in advance of ordinary General Meeting, so that the necessary explanation or information can be ready at the General Meeting. It is thought that this method will be more convenient not only to the shareholder concerned but to all who attend the Meeting." (The Swan Mills, Ltd.)

**7. Supplimentary Information in Balance Sheet.** The following information (not reqnired hy law hnt nsefnl to the reader) is given in the Balance Sheet:—

(a) Share Capital: The details nf rednction nf capital, if any.

(b) Reserves: All reserves (whether general or special) to be shown separately, oone being included in liabilities; and additions to and drawings npon reserves to be given in each case.

(c) Liabilities: The liabilities for nther finance to he amplified.

(d) Loose Tools, Livestock and Stnres: The mode of valnation to be given.

(e) Stock in Trade: The various kinds of stocks snch as raw materials, gnods in process and finished goods to he separately stated and to be valued in a proper manner, i. e., the lower of cost nr market value.

(f) Advances: The amount for which value has to be received and the amount to be recovered in cash to be given separately; and if the amount is large, they are to be classified like book debts.

(g) Investments: The details nl the nature of Investments to he fnrnished and if valued at cost, an idea of the cnrrent market value to be given. Fnrther, investments in two or more subsidiary companies to be separately mentioned. This is very necessary for the pnrpose of ascertaining the values of the holdings in snhsidiary companies.

(h) Cash and Other Balances: The amonnt with the Managing Agents in Current Acconnt to he stated separately.

**8. Proper Grouping.** The various assets and liabilities appearing In the Balance Sheet and the various items nf income aod expenditure appearing in the Profit and Loss Account shonld be properly gronped.

The published accounts of the Kohinoor Mills Company, Limited, for the year 1943 are reproduced as a specimen containing some nf the improvements discnssed above.

THE KOHINOOR MILLS COMPANY, LIMITED.

(97,184 Spindles: 1,134 Looms)

DIRECTORS' REPORT.

The Directors have pleasnre in submitting to the Shareholders their Annnal Report on the affairs nf Compaoy together with the Aodited Acconnts for the year ended 31st December, 1943.

| | | | |
|---|---|---|---|
| The Accounts show that the profit for the year after deductiog depreciation amounting to Rs. 5,41,117 based on the Income Tax statotory allowance is ... ... | | ... Rs. | 1,69,47,750 |
| From this amonot the Directnrs have set aside | | | |
| For Special Depreciation ... | Rs 2,50,000 | | |
| As provision for Taxation ... | „ 1,30,00,000 | | |

| | | | |
|---|---|---|---|
| To cover the estlmated Cnmpulsory Deposit payahle to the Government of India nnder Section 10 of the Firance Act, 1942 by transfers :— | | | |
| To Gereral Reserve | Rs. 11,00,000 | | |
| To Machinery Reserve | Rs. 10,00,000 | | |
| | | „ 21,00,000 | |
| | | | Rs. 1,53,50,000 |
| | | | Rs 15,97,750 |
| *Add*—Balance brought forward frnm last year | | | „ 3,55,965 |
| | | | Rs. 19,53,715 |
| *Less*—Ad-interim dividend paid on 30,000 shares at the rate of Rs. 12/- per share free of Income-tax ... ... | | | „ 3,60,000 |
| Leaving a balance avallable for disposal of ... | | | Rs. 15,93,715 |
| From this sum the Directors recommend the following allocations :— | | | |
| Payment of a final dividend on 45,000 shares at the rate of Rs. 13/- per share free of Income Tax ... | | Rs. 5,85,000 | |
| Payment of a bonns at the rate of Rs. 15/- per share free of Income Tax ... | | „ 6,75,000 | |
| Equalisation of Dividend Fnnd ... | | „ 2,00,000 | |
| Employees' Provident Fnnd | | „ 29,842 | |
| | | | Rs. 14,89,842 |
| Leaving to be carried forward to next year's acconnts ... ... ... | | | Rs. 1,03,873 |

**Trading Conditions.**—Owing to a scarcity of goods brought about by various factors, prices of both cloth and yarn continued to rise throughout the greater part of the year. In Jone Government decided to impose the Cotton Cloth & Yarn (Control) Order with a view not only to controlling the entire nutput of the Indnstry bnt also producing hoarded stocks and thns improving the snpply position generally. Following npon the appointment of the Textile Control Board to advise Government in regard to the Control Order, ceiling prices were fixed by its Chairman for a very great number of different cloths and counts of yarn and the spiral of rising prices was thus hrnnght nnder control to the benefit nf consumers Your Mills again had the advantage nf low priced cotton purchased early in the season and this coupled with the rise in the prices of cloth and yarn mentioned above has resulted in the figures shown in the accompanying accounts which the Directors have no doubt yon will consider satisfactory.

**Depreciation.**—The Directors are strongly nf the opinion that the statutory allowance of one and a half times the single shift rates is

insufficient to cover double shift-working, particularly under wartime conditions and, therefore, in addition to depreciation in accordance with the Statutory Income tax rates amounting to Rs. 5,41,117/- they have set aside a further sum of Rs. 2,50,000/- as Special Depreciation.

**Increase of Capital**.—At an Extraordinary General Meeting of the Shareholders held on the 27th May 1943, the Authorised Capital of the Company was increased from Rs. 30,00,000/- to Rs. 50,00,000/- and subsequently with the consent of the Government of India, 15,000 New Ordinary Shares of Rs. 100/- each were issued at Rs. 100/- premium and have now been fully subscribed. According to the terms upon which the consent was granted, Rs. 30,00,000/- Defence Loan 1953/55 have been purchased in the joint names of the Company and the Secretary, Finance Department and have been deposited with the Chartered Bank of India, Australia & China These funds will be made available when required for the purchase of new machinery.

**Excess Profits Tax**:—The Company's liability to E. P. T. for the period upto 31st December 1942 has been agreed and an optional deposit of Rs. 12,70,567 was made with the Government of India during the year in respect of that period. A further sum of approximately Rs. 21,00,000/- will be payable as a compulsory deposit from the profits of the year 1943 when the Company's Liability to E. P. T. for this year has been agreed and amounts have been set aside to the General and Machinery Reserve Accounts to an equivalent extent.

Under the provisions of Section 10 of the Finance Act, 1942, not only the deposits with interest at 2% p. a. but also Post-war Refunds of E. P. T. will be receivable in due course. No credit has been taken in the accounts for the latter refunds, the gross amount of which in respect of the Excess Profits of the period upto 31st December 1943 are estimated at Rs. 16,50,000.

**Mill Buildings**:—Various alterations and additions including new dispensaries in Nos 1 and 3 Mills were carried out during the year at a cost of Rs. 55,618/-.

**Mill Chawls**:—These continued to be fully occupied throughout the year.

**Mill Air Raid Precautions**:—Under instructions from the A. R. P. Authorities, equipment and structures were provided at a cost of Rs. 38,170/-.

**New Machinery**:—Machinery to the value of Rs. 2,91,867/- was received and erected during the year

**Dearness Allowance**:—The amount paid to mill employees under this heading during the year was Rs. 30,35,092/-. In addition an amount of Rs. 6,81,767/- has been set aside to be paid as bonus for the year 1943.

**Insurance**:—The Mill Property as at 31st December 1943 was insured against loss by fire and all risks arising out of Riots and Civil Commotion for the following amounts :—

| | | | |
|---|---|---|---|
| Building | ... | Rs. | 46,70,600 |
| Machinery | ... | " | 1,20,68,300 |
| Stocks | ... | " | 1,68,74,400 |

The profits and fixed charges have been insured against a stoppage by fire for Rs. 2,00,00,000/-.

Under the Government of India War Risk Insurance Ordinance, the mill stocks as at 31st December 1943 were covered for a sum of Rs. 1,83,00,000/- and the mill buildings and machinery were covered for a sum of Rs. 1,85,59,300/- as at 31st December 1943.

Directorate :—Under Article 107 of the Company's Articles of Association two of the Directors the Hon'ble Sir Shantidas Askuran and Mr. Mafatlal Gagalbhai retire by rotation but are eligible for re-election.

Mr. F. F. Stileman resigned his Office of Ex Officio Director and Chairman on his retirement at the end of June 1943 The Directors have placed on record their deep appreciation of the devoted and outstanding services rendered by Mr. Stileman during his 20 years connection with and as a Director & Chairman of the Company.

On Mr. Stileman's retirement Mr. H. F. Milne was appointed Ex-Officio Director and Chairman in July 1943. On Mr. R. C. Lowndes return from leave in August 1943, he was appointed Ex Officio Director and Chairman and Mr. Milne was invited to join the Board as a Director.

Under Article 98 of the Company's Articles of Association Mr. Milne retains his Office until the General Meeting but is eligible for re-election.

The Directors have recorded with deep regret the death of Mr. H. A. H. Payne which took place on the 8th February 1944. Mr. Payne had been a Director of the Company for nearly 48 years ever since its inception in 1896 and the Board have placed on record their appreciation of the most valuable services rendered by him during his very long association with the Company.

In order to fill the vacancy caused by the death of Mr. Payne the Directors invited Mr. Dinsha K. Daji to a seat on the Board. Mr. Daji retains his office until the General Meeting under Article 98 of the Company's Articles of Association but is eligible for re-election.

*Auditors* :—It is necessary to appoint an Auditor or Auditors and to fix his or their remuneration.

R. C. LOWNDES,

*Chairman,*

*Bombay, 16th February 1944.* On behalf of the Directors.

## THE KOHINOOR MILLS

Balance Sheet as at

| 1942. | CAPITAL AND LIABILITIES. | | |
|---|---|---|---|
| Rupees. | | Rupees. | Rupees. |
| | CAPITAL .— | | |
| | Authorised— | | |
| | 50,000 Ordinary Shares of | | |
| 30,00,000 | Rs 100 each ............ . ... | | 50,00,000 |
| | Issued— | | |
| | 45,000 Ordinary Shares of | | |
| 30,00,000 | Rs. 100 each ........ .. ...... | | 45,00,000 |
| | Subscribed & Called up— | | |
| | 44,970 Shares of Rs. 100 each | | |
| | fully paid ................ .. . | 44,97,000 | |
| | *Less*—Calls in arrears.. ........ | 3,950 | |
| | | 44,93,050 | |
| | New Issue of Shares—Application Deposit against shares | | |
| 30,00,000 | pending allotment...... .. ........ | 1,900 | |
| | | | 44,94,950 |
| | PREMIUM ON SHARES :— | | |
| | As per last account ................. | 12,50,000 | |
| | Due on 14,970 shares of Rs 100 | | |
| | each... ...... ....... ..... .. ... . | 14,97,000 | |
| | | 27,47,000 | |
| 12,50,000 | *Less*—Calls in arrears... ........... | 3,950 | |
| | | | 27,43,050 |
| | RESERVE ACCOUNTS :— | | |
| | General—As per last | | |
| 18,00,000 | Balance Sheet Rs. 22,55,000 | | |
| | Appropriated from | | |
| | the profits of the | | |
| 4,55,000 | year ........... Rs. 11,00,000 | | |
| | | 33 55,000 | |
| 22,55,000 | | | |
| | Machinery—As per last | | |
| ... | Balance Sheet Rs. 10,00,000 | | |
| | Appropriated from | | |
| | the profits of the | | |
| 10,00,000 | year ........ .. Rs. 10,00,000 | | |
| | | 20,00,000 | |
| 32,55,000 | | | 53,55,000 |

COMPANY, LIMITED.

31st December, 1943.

| 1942. | PROPERTY AND ASSETS | | |
|---|---|---|---|
| *Rupees* | | *Rupees.* | *Rupees.* |
| | FIXED CAPITAL EXPENDITURE :— | | |
| 49,49,780 | As per Schedule annexed ...... | | 45,04,305 |
| | STORES, FUEL AND GRAIN— (As per Agents' certified Inventories) ........... ............ ... | | |
| 28,52,122 | | | 32,09,741 |
| | STOCK IN TRADE :— (As per Agents' certified Inventories)— | | |
| 48,61,266 | Cotton, at Cost... Rs. 70,38,316 | | |
| 2,13,279 | Silk and other Yarn at Cost Rs. 4,30 075 | | |
| | | 74,68,391 | |
| 50,74,545 | | | |
| | Cloth, Yarn and Waste— | | |
| 20,19,280 | Sold at contract price, unsold at or below market rate ...... | 21,06,642 | |
| | | | 95,75,033 |
| 70,93,825 | | | |
| | BOOK DEBTS :— | | |
| 11,90,375 | Unsecured and considered good | | 22,48,419 |
| | ADVANCES :— | | |
| 2,92,591 | Insurance premia, rents, taxes, machinery, stores, etc........... | | 2,38,967 |
| | DEPOSITS :— | | |
| | 2% Deposit (with Government of India under Section 10 of the Finance Act 1942) .............. | 12,70,567 | |
| | Against machinery ordered ...... | 66,783 | |
| 5,000 | With East India Cotton Association, Ltd.......................... | 5,000 | |
| | | | 13,42,350 |

| 1942 | | Rupees. | Rupees |
|---|---|---|---|
| Rupees | LOANS UNSECURED :— | | |
| 10,09,619 | Fixed Deposits.................. ..... | 4,80,813 | |
| 10,282 | Interest accruing but not due.. ... | 2,407 | |
| | | | 4,83,220 |
| 10,19,901 | | | |
| 12,652 | UNCLAIMED DIVIDENDS ...... | | 10,182 |
| | LIABILITIES :— | | |
| 5,91,617 | For Goods supplied ......... ........ | 6,55,974 | |
| 17,89,178 | ,, Expenses (including provision for Agents' Commission) | 22,96,502 | |
| 95,013 | ,, Other finance............. ... | 1,05,375 | |
| 64,92,632 | ,, Provision for taxation... ... | 1,28,47,035 | |
| | | | 1,59,04,886 |
| 89,68,44[illegible] | | | |
| | ADVANCES :— | | |
| 1,76,229 | From Selling Agents, Chawls Rent, Waste, etc. .................. | | 1,05,263 |
| | PROFIT AND LOSS :— | | |
| 12,24,182 | Balance as per Appropriation Account annexed ........ ..... .. | | 15,93,715 |
| | NOTE:—No account has been taken of Post War Refunds of E. P T in respect of the optional deposits made for the years ended 31st December, 1941 and 1942, and the compulsory deposit to be made from the profits of the year ended 31st December 1943. The aggregate amount of the refund for these three years is estimated at Rs. 16,50,000 in respect of which Income Tax and Super Tax as well as Commission to the Agents will be payable in the year of receipt. | | |
| 1,89,06,404 | Total Rupees | | 3,06 90,266 |

| Rupees. | | Rupees. | Rupees |
|---|---|---|---|
| | INVESTMENTS—at Cost :— | | |
| 9,40,312 | 3½% Government Loan of Rs. 10,00,000.......... | 9,40,312 | |
| | 3% Government Loan 1951/54 of Rs 10,00 000.......... | 10,00,000 | |
| | 3% Defence Loan 1953/55 of Rs. 30,00,000 in joint names of the Company and the Secretary, Finance Dept.. Govt. of India .......... | 30,00,000 | |
| | Treasury Bills .......... | 22,45,782 | 71,86,094 |
| 4,466 | INTEREST ACCRUED ON INVESTMENTS & DEPOSITS..... | | 65,986 |
| | CASH & BANK BALANCES:— | | |
| 15,77 508 | With Banks on Current Account | 23,18,808 | |
| 425 | In hand .......... | 563 | 23,19,371 |
| 15,77,933 | | | |
| 1,89,06,404 | Total Rupees. | | 3,06,90,256 |

THE KOHINOOR MILLS

Schedule of Fixed Capital Expenditure attached to and forming

| Description of Assets. | COSTS. | | | |
|---|---|---|---|---|
| | To 31st Dec., 1942 | Additions during the year. | Transfers during the year. | Sub-Total. |
| | Rupees. | Rupees | Rupees. | Rupees. |
| LAND:— | | | | |
| Freehold | 2,42 595 | ... | ... | 2,42,595 |
| Leasehold | 1,131 | ... | ... | 1,131 |
| BUILDINGS:— | | | | |
| Spinning, Weaving and Transformer Houses | 24,39,947 | ... | ... | 24,39,947 |
| Offices, Residential Quarters, Dispensaries, Godowns and Compound Walls | 2,93,428 | 52,086 | ... | 3,45,514 |
| Chawls | 12,91,096 | ... | ... | 12,91,096 |
| Workmen's Institute | 20,315 | ... | ... | 20,315 |
| Dyeing and Bleaching Houses | 4,40,200 | 3,532 | ... | 4,43,732 |
| MACHINERY:— | | | | |
| Spinning, Weaving, Waste, Humidifier and Sprinkler Installations and Fire Service | 77,27,392 | 2,69,027 | −4,109 | 79,92,310 |
| Dyeing and Bleaching | 7,22,775 | 5,184 | ... | 7,27,959 |
| Electric Light Installations, Cable Equipment and Electrical Equipment | 7,86,808 | 16,997 | ... | 8,03,805 |
| Artificial Silk | 3,10,420 | 659 | +4,109 | 3,15,188 |
| *MOTOR CARS & LORRIES* | 24,469 | ... | ... | 24,469 |
| FURNITURE, TYPEWRITERS & CALCULATING MACHINES | 32,091 | 2,136 | ... | 34,227 |
| Total. | 1,43,32,667 | 3,49,621 | ... | 1,46,82,288 |

COMPANY, LIMITED.

part of the Balance Sheet as at 31st December, 1943

| Deductions Sales, etc. during the year. | Gross Block as at 31-12-1943 | DEPRECIATION WRITTEN OFF. To 31st Dec. 1942. | Deductions | Transfers. | Sub-Total | From the Profit of 1943. | To 31st Dec. 1943. | Balance as at 31st Dec. 1943. |
|---|---|---|---|---|---|---|---|---|
| Rs. | Rupees. | Rupees. | Rs. | Rupees. | Rupees | Rupees. | Rupees. | Rupees. |
| .... | 2,42,595 | ... | ... | ... | ... | ... | .. | 2,42,595 |
| ... | *1,131* | ... | ... | ... | ... | ... | ... | *1,131* |
| ... | 24,39,947 | 12,38,130 | ... | ... | 12,38,130 | 47,016 | 12,85,146 | 11,54 801 |
| ... | 3,45,514 | 48,633 | ... | ... | 48,633 | 7,422 | 56,055 | 2,89,459 |
| ... | 12,91,096 | 8,45,269 | ... | ... | 8,45 269 | 17,683 | 8,62,952 | 4,28,144 |
| — | 20,315 | 11,020 | ... | ... | 11,020 | 232 | 11,252 | 9,063 |
| ... | 4,43,732 | 1,77,426 | ... | ... | 1,77,426 | 13,315 | 1,90,741 | 2,52,991 |
| ... | 79,92,310 | 57,76,316 | ... | −3,41[illegible] | 57,72,897 | 4,69,325 | 62,42,222 | 17,50,088 |
| ... | 7,27,959 | 5,14,16[illegible] | ... | ... | 5,14,162 | 79,622 | 5,93,784 | 1,34,175 |
| ... | 8,03 805 | 6 48,843 | ... | ... | 6,48,843 | 68,898 | 7 17,741 | 86 064 |
| 7,400 | 3,07,788 | 96,329 | 3,421 | +3,419 | 96,327 | 83,738 | 1,80 065 | 1,27,723 |
| ... | 24,469 | 15,435 | ... | ... | 15,435 | 1,840 | 17,275 | 7,194 |
| ... | 34,227 | 11,324 | ... | ... | 11,324 | 2,026 | 13,350 | 20,877 |
| 7,400 | 1,46,74,888 | 93 82,887 | 3,421 | ... | 93,79,466 | *7,91,117 | 1,01,70,583 | 45,04,305 |

*Includes Rs. 2,50,000 Special Depreciation.

THE KOHINONR MILLS

Dr. Profit and Loss Account for the

| 1942. Ropees. | | Rupees. | Rupees. |
| --- | --- | --- | --- |
| 60,78,092 | To Cotton-Stock on 31st Dec., 1942 | 48,61,266 | |
| 85,09,662 | *Add*—Pnrchases ................ | 1,65,43,962 | |
| 1,45,87,754 | | 2.14,05,228 | |
| 48,61,266 | *Less*—Stock on 31st Dec., 1943 | 70,38,316 | |
| | | | 1,43,66,912 |
| 97,26,488 | | | |
| 95,541 | „ Muccadamage & Cotton Cess... | | 95 552 |
| | „ Silk & other Yarn:— | | |
| 4,98,511 | Stock on 31st December, 1942 | 2,13,279 | |
| 11,15,043 | *Add*—Purchases ................ | 22,68,348 | |
| 16,13,554 | | 24,81,627 | |
| 5,07,804 | *Less*—Sales ...................... | 1,288 | |
| 11,05 750 | | 24,80,339 | |
| 2,13,279 | *Less*—Stock on 31st Dec., 1943 | 4,30,075 | |
| | | | 20,50,264 |
| 8,92,471 | | | |
| 5,28,001 | To Yarn & Cloth Commissions ... | | 8,15,513 |
| 3,10,962 | „ „ „ „ Expenses...... | | 4,16,208 |
| | „ Stores, Fnel & Repairs:— | | |
| 19,38,552 | Stock on 31st December, 1942 | 27,26,251 | |
| 35,73,088 | *Add*—Purchases ............... | 42,87,370 | |
| 55,11,640 | | 70,13,621 | |
| 27,26,251 | *Less*—Stock on 31st Dec., 1943 | 31,43,545 | |
| | | | 38,70,076 |
| 27,85,389 | | | |
| 4,75,385 | To Electric Power ..................... | | 4,87,226 |
| 43,10,459 | „ Salaries & Wages (including interim allowance) .............. | 44,34,196 | |
| 12,56,580 | „ Dearness allowance ............... | 30,35,092 | |
| | | | 74,69,288 |
| 55,67,039 | | | |
| 1,20,460 | „ Millhands Welfare Expenses... | | 34,976 |
| 2,09,977 | „ Rents & Taxes (including Rs. 26,873-2-0 for Urban Immovable Property Tax)...... | | 2,38,686 |

COMPANY, LIMITED.

Year Ended 31st December, 1943. Cr.

| 1942 Rupees. | | Rupees. | Rupees. |
|---|---|---|---|
| 3,16,70,718 | By Cloth, Yarn & Waste Sales ... | 4,90,66,159 | |
| 18,35 681 | *Less*—Stock on 31st Dec., 1942 | 20,19,280 | |
| 2,98,35,037 | | 4,70,46,879 | |
| 20,19,280 | *Add*—Stock on 31st Dec., 1943 | 21,06,642 | 4,91,53,521 |
| 3,18,54,317 | | | |
| 4,958 | By Transfer Fees .................. | | 5,288 |
| 2,576 | ,, Interest .. . ... .................... | | 82,425 |
| 30,506 | ,, Miscellaneous Receipts ......... | | 25,318 |
| 59,572 | ,, Chawls Revenue—Rent ........ | 59,730 | |
| 48,(76 | *Less*—Upkeep ......... ... .... | 59,404 | 326 |
| 11 496 | | | |

| Rupees. | | Rupees. | Rupees. |
|---|---|---|---|
| 87,868 | To Insnrance ........................ | 1,43,469 | |
| 6,05,238 | ,, War Risk Insurance ............ | 7,41,746 | |
| 6,93,106 | | | 8,85,215 |
| 5,918 | To General Brokerage ............... | | 2,924 |
| 30,664 | ,, Advertising, Printing and Stationery ......................... | | 67,782 |
| 8,495 | ,, Auditors' & Directors' Fees ... | | 11,355 |
| 1,27,829 | ,, Interest ................................ | | 43,949 |
| 22,470 | ,, General Charges .................. | 28,719 | |
| 76,674 | ,, A. R. P. Expenses ...... .... ... | 38,170 | |
| 99,144 | | | 66,889 |
| 5,591 | To Trade Subscriptions.. ...... ... | | 6,103 |
| 19,275 | ,, Motor Cars & Lorries Expenses | | 23,035 |
| | ,, Agents' Remnneration :— | | |
| 6,000 | Office Allowance.................. | 6,000 | |
| 5,27,267 | Commission on profits (Subject to final adjustment in respect of Excess Profits Tax)......... | 8,15,835 | 8,21,835 |
| 10,924 | Commission on purchases debited to Capital Expenditure ......... ...................... | 8,527 | |
| 5,44 191 | | 8,30,362 | |
| 5,74,717 | To Depreciation ........................ | | 5,41,117 |
| 90,94,134 | ,, Balance, being profit, carried down ................................ | | 1,69,51,973 |
| 3,19,03,853 | Total. | | 4,92,66,878 |

Dr. PROFIT AND LOSS ACCOUNT FOR THE

| 1942. Rupees. | | Rupees. | Rupees. |
|---|---|---|---|
| 7,972 | To Donations .. ................. ..... | | 30,394 |
| 2,00,000 | „ Special Depreciation ... ........ | | 2,50,000 |
| 64,11,676 | „ Provision for taxation...... .. | | 1,30,00,000 |
| | „ Reserve Accounts (Estimated amount required for compulsory deposit with Government) | | |
| | General ........................ .. | 11,00,000 | |
| 10,00,000 | Machinery ..................... .. | 10,00,000 | 21,00,000 |
| 14 82,660 | „ Balance carried down to Appropriation Account ... ........ | | 15,97,750 |
| 91,02,308 | Total Rupees. | | 1,69,78,144 |

Dr. APPROPRIATION ACCOUNT

| Rupees. | | Rupees. | Rupees. |
|---|---|---|---|
| 4,49,998 (15%) | To Final Dividend for the year ended 31st December, 1942 at the rate of Rs 13/- per share free of Income-tax ...... | | 3,90,000 |
| 3,59,999 (12%) | „ Bonus for the year ended 31st December, 1942 at the rate of Rs. 15/- per share free of Income-tax .............. | | 4,50,000 |
| 27,784 | „ Employees' Provident Fund ... | | 28,217 |
| 1,01,522 | „ Balance carried down............ | | 3,55,965 |
| 9,39,303 | | | 12,24,182 |
| 3,60,000 | To Ad-interim Dividend paid on 14-9-43 at the rate of Rs 12/ per share free of Income-tax... | | 3,60,000 |
| 12,24,182 | „ Balance carried to Balance Sheet ................ ............ | | 15,93,715 |
| 15,84,182 | Total Rupees | | 19,53 715 |

**Report of the Auditors to the Shareholders.—**

We have audited the foregoing Balance Sheet of The Kohinoor Mills Company, Limited, as at 31st December, 1943, and also the foregoing Profit and Loss Account of the Company for the year ended upon that date, and report that:—

*(a)* we have obtained all the information and explanations we have required ;

*(b)* in our opinion, the forgoing Balance Sheet and Profit and Loss Account are drawn up in conformity with the law ;

*(c)* such Balance Sheet exhibits a true and correct view of the state of the Companys' affairs according to the best of our information and the explanations given to us and as shown by the books of the Company, and

*(d)* in our opinion, books of account have been kept by the Company during the period under report as required by Section 130 of the Indian Companies Act, 1913.

*Bombay,* A. F. FERGUSON & Co.,
*11th February, 1944.* Chartered Accountants, Registered Accountants.

YEAR ENDED 31st DECEMBER, 1940—(Concld.) Cr.

| 1942. Rupees. | | Rupees. | Rupees. |
|---|---|---|---|
| 90,94,134 | By Balance brought down........... | | 1,69,51,973 |
| 28,174 | „ Profit on sale of Machinery ... | | 26 171 |
| 91,02,308 | Total Rupees | | 1 69,78 144 |

AS AT 31st DECEMBER, 1943. Cr.

| Rupees | | Rupees | Rupees. |
|---|---|---|---|
| 9,39,303 | By Balance as per last Balance Sheet .............................. | | 12,24,182 |
| 9,39,303 | | | 12,24,182 |
| 1,01,522 | By Balance brought down......... .. | | 3,55 965 |
| 14,82,660 | „ Balance brought down from the Profit & Loss Account of the year ........ ... . ........ .. | | 15,97,750 |
| 15,84,182 | Total Rupees, | | 19,53,715 |

R. C. LOWNDES, *Chairman.*

PURSHOTAMDAS THAKURDAS,
MAFATLAL GAGALBHAI,
M. S. CAPTAIN,
H. F. MILNE,
DINSHA K. DAJI
*Directors.*

KILLICK NIXON & CO.,
*Agents.*

## CHAPTER 8

### CRITICISM OF PUBLISHED ACCOUNTS.

It has already been pointed out in the preceding chapters that the term 'Published Accounts' refers to the balance sheet, the profit and loss account, the directors' report, and the auditor's report of a company together with a copy of the chairman's statement. Where a company happens to be a holding company, its published accounts also include the balance sheet, the profit and loss account and the auditor's report of each subsidiary and sub-subsidiary company. The shareholders of a company are therefore supplied with sufficient information concerning its working and its financial position, so that they may easily ascertain the value of their investments. This they can do only when they understand how to make use of such published accounts; and it is the purpose of this chapter to explain how the published accounts of a company may be read and understood.

The persons who are primarily interested in the affairs of a company are its shareholders—present and prospective. The existing shareholders of a company may be placed into four distinct groups. There are those who will stick to the company through thick and thin—the permanent investors who will hold their shares till the last trump. Secondly, there are the speculative investors who have taken up semi-permanent residence, but mean eventually to get out at a profit. Thirdly, there are speculators, pure and simple, who are here to day and gone tomorrow. Finally, there are silent interests who prefer to hide their identity under nominees, and have their eye on some move in a big strategic campaign Parkinson : *Scientific Investment.*

Besides the shareholders, the creditors of a company are also interested in its published accounts. But it must be recognised that if the affairs of a company are considered to be satisfactory from the point of view of its shareholders, then they must be regarded as more satisfactory from the point of view of its creditors, because the latter have a prior claim on the company's assets. It is now proposed to describe how the published accounts of a company may be examined from the point of view of its ordinary shareholders.

*What is Criticism?* The term 'Criticism' means a thorough examination of the published accounts for some purpose, e. g., to ascertain the value of the investment of ordinary shareholders in a company. Criticism is an art which can be exercised only when suitable material is available. The criticism of published accounts may be of two kinds.

#### 1. Criticism of Form

The criticism of the form of published accounts implies an examination of their contents with a view to ascertaining whether or not the information disclosed therein is in conformity with the requirements of law, i. e., the requirements of the Indian Companies Act and the Indian Insurance Act. This duty is expressly imposed by section 145 of the Indian Companies Act upon the company's auditors who have to

state in their audit report to its members whether or not in their opinion the Balance Sheet and the Profit and Loss Account (or Revenue Accounts in the case of Insurance Companies) audited by them are drawn up in conformity with the law. Therefore, those who are interested in the published accounts of companies may take it for granted that, if the auditors' report is unqualified, the accounts are correct in form.

In spite of this precaution, it may, however, sometimes be found that the published accounts are defective in one respect or another although the auditors' report says that they are in conformity with the law. Such cases are, of course, rare; but they do exist. Here are a few examples taken from the actual published accounts of Indian companies, and it may be stated that in each case the auditors have given a clean report.

1. **The Sitalpore Sugar Works, Ltd.** In the Balance Sheet as on 30th June 1939 the mode of valuation of the Company's stock is not stated; and in the Profit and Loss for the year ended on that date the directors' fees are not separately stated. The same mistakes are repeated in the next year's accounts as well.

2 **The Orient Paper Mills, Ltd.** In the Balance Sheet as on 31st March 1943 the Company's investments are stated simply as 'Shares and Securities' without disclosing their nature and mode of valuation.

3. **The Kohinoor Mills Co., Ltd.** In the Profit and Loss Account of the Company for the year ended 31st December 1943 the directors' fees are not separately stated, but they are given coupled with auditors' fees.

4. *The Mettur Chemical and Industrial Corporation, Ltd.* In the Profit and Loss Account of the Company for the year ended 31st March 1945 Rs. 2,92,689 being depreciation of machinery was included in the item 'Cost of Production' and was not shown separately, although the law expressly requires that the total amount of depreciation should be given as a separate item in the profit and loss account.

It is also found that in many cases the directors' reports attached to the published balance sheets do not contain all the information required by section 131—A.

### 2. Criticism of Substance

The criticism of the substance of published accounts of a company involves a critical analysis of their contents with a view to forming an opinion on the value of its business for the guidance of its present and prospective shareholders and creditors. This type of criticism is not an easy matter. It demands a searching ability on the part of the reader.

When a medical practitioner is asked to make an examination of the body of a human being, he knows what tests to apply with a view to finding out the state of health of the person concerned. He carefully examines the heart, the lungs, the pulse, and so on. He then expresses his opinion regarding the health of the patient. By what criteria should the published accounts of a company be examined in order to ascertain the value of its business? The criteria to be applied may be expressed by three P's—*progress, position* (i. e., financial position) and *prospects.* How each of these three tests may be applied will now be explained in detail.

### I. The Company's Progress.

In order to measure the progress of a company from its published accounts, it is necessary to examine the profit and loss account, the directors' report and the chairman's speech for a number of years. It is dangerous to examine the profit and loss account figures of only a year or two. *If a reliable idea of a company's progress is to be* gathered, the profit and loss account for a period of three to five years should be examined. The profit and loss account as published from year to year cannot, however, enable the reader to obtain the reqnisite information at a glance. For this purpose he must prepare a comparative analysis of the profit and loss account for the period covered by his examination. The analysis showing the statistical information about the company's earnings and dividend record will then easily enable him to draw his conclnsions.

In preparing the statistical analysis, it must be borne in mind that the requisite information is presented in a lucid manner. Sir G. S. Bajpai, in the course of his presidential speech at the Indian Statistical Conference, held in January 1941 at Benares, rightly pleaded for a lucid presentation of statistics in a manner which will be easily understood by the people at large. "A science which can only survive through popular recognition," he said, "cannot afford to be esoteric."

The published profit and loss account of a company contains a lot of useful information; but unless it is broken up, analysed and essential features presented in a lucid manner, it cannot tell the reader what he wants to know about the company's working. The statistical information found in the published profit and loss accounts and the directors' reports of a company for a number of years may, therefore, be analysed and presented in a comparative form as follows:—

**Analysis of Working.**

| | Year ended 31st December | | | | | |
|---|---|---|---|---|---|---|
| | 1941 | 1942 | 1943 | 1944 | 1945 | |
| | Rs. | Rs. | Rs | Rs. | Rs. | |
| Sales ... | | | | | | |
| Other Income ... | | | | | | |
| Closing Stock ... | | | | | | |
| Manufacturing Expenses ... | | | | | | |
| Managing Agents' Remuneration | | | | | | |
| Other Expenditure ... | | | | | | |
| Gross Profit ... | | | | | | |
| Percentage of Gross Profit to Sales ... | | | | | | |
| Depreciation ... | | | | | | |
| Taxation ... | | | | | | |
| Net Profit ... | | | | | | |
| Written off past Losses ... | | | | | | |
| Transfers to Reserves ... | | | | | | |
| Other Parties' Shares ... | | | | | | |
| Amount available for dividends | | | | | | |
| Dividends :— ... | | | | | | |
| Peference Amount | | | | | | |
| % | | | | | | |
| Ordinary Amount | | | | | | |
| % | | | | | | |
| Deferred Amount | | | | | | |
| % | | | | | | |
| Carry-forward | | | | | | |

This analysis is suitable for a manufacturing company. The analysis of the profit and loss accounts of other companies (e. g., banking companies, investment trusts, coal mines, tea companies and others) will be given later on.

In order to prepare this comparative statement showing the results of a company's working, the following points must be borne in mind :—

1. The analysis is compiled from the published profit and loss accounts and the directors' reports for the period covered by the examination after giving effect to the appropriations made or recommended by the directors. The appropriations of profit proposed by the directors will probably have been sanctioned by the shareholders in general meeting before the results in most cases come up for examination before the public.

2. If the period covered is long, say five years, and if the figures involved are large, the analysis may be made in thousands of rupees, taking each item to the nearest thousand. Thus Rs. 87,23,456 may be taken as Rs. 87,23. Where this method is adopted, a note of the fact must be made at the top of the table, e. g., (In thousands of rupees). If the same thing is expressed in lakhs of rupees, then a decimal point will be used in place of the comma—thus Rs. 87.23 instead of Rs 87,23.

3. In many cases the stocks appearing in the published profit and loss account are those of manufactured goods only, the stocks of raw materials and stores being adjusted into the manufacturing expenses; and in a few cases (The Muir Mills Co., Ltd., of Cawnpore and the Nutan Mills, Ltd., of Ahmedabad, for example) no stocks of any kind are given in the profit and loss account. Where the stocks consist only of manufactured goods, this fact should be noted in the statement against the item of closing stocks; and where even the stocks of finished goods do not appear in the profit and loss account, they must have been adjusted into the figure of sales, and it will therefore be unnecessary to include the stocks in the analysis.

4. In some concerns, such as light railway companies, there are no sales as such, and therefore the gross income consists of other items, e. g., passenger and goods earnings, etc.

5. If apart from sales, there is any other substantial source of gross income such as interest from investment, profit from the sale of investments, profit from the sale of a capital asset, and the like, it should be given separately in the analysis and not merged with 'Other income'.

6. The managing agents, particularly in the case of some of the cotton mill companies of Bombay and Ahmedabad, are entitled to commission on profits as well as on the purchases of stores and capital assets. Part of such total remuneration is debited to stores and to capital accounts and the balance only to profit and loss account. Only that part of the managing agents' remuneration which is debitable to the profit and loss account will appear in the analysis; but it is essential that the remuneration payable to the managing agents which has been charged to stores and capital accounts should also be shown by way of a footnote on the analysis, so that the total amount payable to them may be known.

7. Should there be any substantial expenditure of a special nature (e. g., excise duty, loss on the sale of a fixed asset and the like), it should be mentioned as a separate item in analysis and not merged in the item of other expenditure.

8. The amount of depreciation shown in the analysis may also include any sums written off nominal assets such as discount on debentures, preliminary expenses, etc., and also any loss on the sale of fixed assets and any amount written off on reduction of capital. But this fact must be made clear by means of a footnote Moreover, if the provision for depreciation made in any year is not only on account of that year but also on account of any past arrears this fact should be stated by a footnote.

9. If any excess taxation provision made in one year is taken into account in another year, this fact should be referred to in a foot note. If no separate provision is made for the taxation liability, but the amount needed for that purpose is left in the carry forward, a note to that effect is also necessary at the foot of the analysis.

10. All reserves created out of net profits will appear in the analysis ; but if any particular reserve is built up out of other surpluses (e. g., Investment Reserve Account set up out of profits made on the sale of investments), this fact should be referred to in a footnote.

11 The profits of certain companies belong not only to their shareholders but also to some third parties. For example, the profits of some light railway companies are shared either by the district boards or by Government, and similarly a portion of the profits of the Steel Corporation of Bengal, Ltd., goes to the Indian Iron and Steel Co., Ltd. In such cases, before arriving at the profits available for dividend, the share of profits to which other parties are entitled has to be given separately in the analysis.

12. Should there be gross loss instead of gross profit or net loss instead of net profit, or should there be any transfers made from past reserves instead of amounts transferred to reserves, then these facts must be indicated in the analysis by placing the sign of a minus ( - ) against the amounts concerned.

13. If the accounts are prepared annually and if there has been any interim distribution, the amount of the interim dividend should be shown along with the amount of the final dividend, and the fact is referred to in a footnote. Where the accounts are made up half yearly, the dividends given in the analysis will be for each half-year. Where the dividends declared on preference shares in any year include the past arrears, or where the dividends on ordinary shares include any bonus distribution, these facts are stated in a footnote. If there has been any increase of paid up capital, the dividend should be related to the capital by means of a footnote such as 'Dividend paid on a capital of Rs. 30,00,000 as against Rs. 20,00,000 in 1944.'

14. In some cases the analysis of working must be supplemented by statistical data about production, etc Thus, the statement of working of a sugar mill company may include figures relating to cane crushed in maunds, sugar made in maunds and the yield per cent. on cane used ; that of a coal company the raisings and despatches in tons ; and

that of a tea company the acreage under crop, the out turn in lbs. and the average selling price per lb.

15. Where the method of preparing the profit and loss account differs from year to year, care must be taken to see that the figures for the various years covered by the analysis are properly adjusted so that the same factors may be taken into consideration.

Given below are a few specimen analyses of the working results of companies engaged in different trades and industries, and these (except the last one) have all been taken from the columns of the *Commerce*.

**1. The Svadeshi Mills Co., Ltd.**

The salient featnres of the Company's results for the year under review are set out in the following comparative table :—

*(In thousands of rupees)*

| | Year ended 31st December | | | | |
|---|---|---|---|---|---|
| | 1940 | 1941 | 1942 | 1943 | 1944 |
| | Rs. | Rs. | Rs. | Rs. | Rs |
| Sales ... ... | 52,34 | 1,00,98 | 1,58,09 | 3,13,58 | 3,07,36 |
| Stocks* .. ... | 16,29 | 30,19 | 35,53 | 49,63 | 48,54 |
| *Value of cotton consumed* | *22,30* | *37,55* | *45,30* | *88,81* | *1,02,50* |
| Manufacturing charges only ... ... | 26,97 | 46,31 | 59,27 | 97,33 | 98 85 |
| Agents' commission ... | 37 | 2,56 | 5,04 | 12,69 | 9,13 |
| Profit† ... ... | 4.23 | 23,02 | 45,17 | 1,13,70 | 82,10 |
| Provision for— | | | | | |
| Depreciation ... | 1,00 | 3,00 | 4,00 | 5,00 | 4,00 |
| Taxation ... ... | 5 | 13 35 | 30,25 | 84,00 | 61,00 |
| Net profit ... ... | 3,18 | 6,67 | 10,92 | 24,70 | 17,10 |
| Transfer to— | | | | | |
| Reserve fund .. | ... | 1,00 | 1,00 | 13,43 | 9,90 |
| D. E. Fund ... | ... | 1,00 | 1,50 | — | — |
| Dividends— | | | | | |
| 5% Preference ... | 75 | 75 | 75 | 75 | 75 |
| Ordinary‡ ... ... | 1,40 (7%) | 3,60 (18%) | 7,50 (25%) | 10,50 (35%) | 6,60 (22%) |
| Carry-forward ... | 3 | 35 | 52 | 55 | 40 |

*Stocks of yarn, cloth and waste

†Profit arrived at after meeting all expenses including Agents' commission but before providing for taxation and depreciation.

‡The distribution to shareholders for 1942, 1943 and 1944 include a bonus of 7 per cent., 15 per cent. and 6 per cent. respectively.

2. **The Kesoram Cotton Mills, Ltd.**

The following comparative table will enable one to get at a glance a better idea of the improvement in the results of the company for the half-year under review.

(Value in thousands of rupees)

| | | Half year ended | | | |
|---|---|---|---|---|---|
| | | 30-9-'43 | 31-3-'43 | 30-9-'42 | 30-9-'41 |
| | | Rs. | Rs. | Rs | Rs. |
| Sales | ... | 178,70 | 146,71 | 79,86 | 93,82 |
| Closing stock | ... | 19,56 | 21,64 | 22 27 | 10,23 |
| Working expenses | ... | 137,79 | 112,37 | 67,20 | 65,55 |
| Gross profit | ... | 38 82 | 33,70 | 21,13 | 16,30 |
| Provision for— | ... | | | | |
| Taxation | ... | 21,00 | * | * | 4,00 |
| Depreciation | ... | 3,38 | 3,13 | 3,75 | 3,01 |
| Net profit | ... | 5,76 | 23.83† | 12,30† | 5,06 |
| Dividend— | ... | — | | | |
| 7% preference | ... | 70 | 70 | 70 | 70 |
| Ordinary | ... | 4,00 | 4,00 | ‡ | 3,00 |
| Do % p. a. | ... | (40%) | (40%) | | (40%) |
| Transfer to reserve | .. | *Nil* | *Nil* | *Nil* | 100 |
| Carry forward | ... | 3,01 | 1,95§ | 11,82† | 46 |

*No separate provision was made.

†Subject to provision for taxation.

‡No dividend was paid but bonus shares were issued by capitalising Rs. 5 lakhs out of the reserve fund.

§This has been arrived at after setting apart Rs. 29 lakhs to taxation for the year ended 31st March, 1943.

A straight comparision of the net profit, dividend, and other allocations for the half-year under review with those for the corresponding half-year is rendered difficult owing to the change in the method of presenting accounts and also the increase in capital brought about by capitalisation of a portion of the reserves.

3. **The Hindusthan Sugar Mills, Ltd.**

The following comparative table provides striking testimony to the progressive improvement in the working results of the Company in the last four years ;—

| | Year ended 30th June | | | |
|---|---|---|---|---|
| | 1944 | 1943 | 1942 | 1941 |
| | Rs. | Rs. | Rs | Rs. |
| Sale of sugar ... | 69,70,216 | 67,59 791 | 46,93,949 | 37,96,047 |
| Profit on farms ... | 1,37,372 | 1,46,592 | 18 077 | 10,514 |
| Excise duty ... | 10,59,036 | 9,23,220 | 11,74,269 | 4,05,131 |
| Profit* — | 15,37,121 | 15 41,076 | 11,20,544 | 4 91,437 |
| Agents' commission and allowance ... | 1,53,062 | 1 52,048 | 1,17,344 | 57,100 |
| Bonus to employees ... | 1,14,505 | 1,07,373 | 37,102 | 17,000 |
| Provision for— | | | | |
| Depreciation ... | 1,50,000 | 1,50,000 | 1,50,000 | 2,00,000 |
| Taxation ... | 4,50,000 | 4,35,000 | 2 60,000 | 60,000 |
| Reserve fund ... | 5,00,000 | 5,00,000 | 3,85,000 | 50 000 |
| Charity ... | 15,000 | 27,761 | 5,000 | 5,000 |
| Dividends— ... | | | | |
| 5% cum Pref. ... | 25,000 | 25,000 | 25,000 | 25,00ɹ |
| Ordinary ... | 1,50,000 | 1,25,000 | 1,00,000 | 60,000 |
| | (15%) | (12½%) | (10%) | (6%) |
| Carry forward ... | 7,927 | 28,372 | 30,700 | 7,602 |

*Before providing for taxation, depreciation, Agents' commission, and bonus to employees but after meeting all other expenses.

4. **The Bengal Coal Co., Ltd.**

*(Value in thousands of rupees)*

| | Half year ended | | | |
|---|---|---|---|---|
| | 30-4-1945 | 31-10-1944 | 30-4-1944 | 31-10-1943 |
| | Rs. | Rs | Rs. | Rs. |
| Sales of coal ... | 1 96,38 | 1,64,81 | 98,95 | 78,05 |
| Other income ... | 4,90 | 4,51 | 3,78 | 3,56 |
| Stock ... | 7,48 | 7,88 | 5,33 | 1,64 |
| Coal purchases ... | 80,26 | 64,17 | 26,75 | 15,23 |
| Working expenses ... | 63,98 | 52,54 | 51,34 | 44 34 |
| Gross profit ... | 51,63 | 55 16 | 28,33 | 18,13 |
| Transfer to :— | | | | |
| Taxation and cess reserve ... | 40,30 | 38,00 | 17,66 | 9,25 |
| Depreciation ... | 3,00 | 3,00 | 3,00 | 3,00 |
| Reserves ... | 2,00 | 3,25 | ... | ... |
| Dividend ... | 20% p. a. | 20% p. a. | 20% p. a. | 20% p. a. |
| Bonus to shareholders ... | 16% p. a. | 12% p. a | 4% p. a. | 4% p. a. |
| Carry forward ... | 2,78 | 2,72 | 1,83 | 96 |
| | Tons | Tons | Tons | Tons |
| Raisings ... | 8,11 | 7,23 | 7,63 | 7,84 |
| Despatches ... | 13,55 | 11,91 | 9,13 | 9,89 |

**The Patrakola Tea Co., Ltd.**

Table showing the progress of the Company during the last three ars :—

| | Year ended 31st December | | |
|---|---|---|---|
| | 1940 | 1939 | 1938 |
| | Rs. | Rs. | Rs. |
| e proceeds ... | 26,29,617 | 24,79,583 | 20,10,462 |
| penditure ... | 15,06,345 | 15,28,006 | 13,82,740 |
| ss profit ... | 11,26,251 | 9,53,656 | 8,33,261 |
| ation reserve ... | 2,25,000 | 2,27,500 | 90,000 |
| profit ... | 9,95,430 | 8,23,963 | 8,40,821 |
| idend ... | 72½ | 62½ | 65 |
| ry forward ... | 5,19,308 | 4 36,343 | 4,19,857 |
| a planted (in acres) ... | 5,799 37 | 5,799.37 | 5,799.37 |
| l crop (in mds,) ... | 53,634 | 57,460 | 53,742 |
| rage sale price per lb. ... | As. 9·7 | As. 8·5 | As. 8 2 |
| enditure per lb ... | As. 5·9 | As. 5·7 | As. 5·5 |
| it per lb. ... | As. 3 10 | As. 2·11 | As. 2 10 |

**The Bank of India, Ltd.**

We give below a comparative table which shows at a glance the essive results of the Bank for the year under review :

(In thousands of Rupees)

| | Year ended 31st December | | | |
|---|---|---|---|---|
| | 1944 | 1942 | 1941 | 1940 |
| | Rs. | Rs. | Rs. | Rs. |
| st and discount earned ... | 79,36 | 62,06 | 60 96 | 58,72 |
| st and discount allowed .. | 14,73 | 16,95 | 20,03 | 23,25 |
| ission and exchange earned | 5,07 | 3 96 | 3,09 | 2,45 |
| gross income ... | 84,96 | 66 51 | 64,39 | 61,67 |
| nistrative expense ... | 27,22 | 22,83 | 20,22 | 18,83 |
| ... | 43,01 | 26,73 | 24,13 | 19,59 |
| end ... | 12% (12,00) | 12% (12,00) | 11% (11,00) | 11% (11,00) |
| ion for— | | | | |
| tion ... | 15,00 | 6,00 | 4,00 | 2,50 |
| rve fund ... | 2,50 | 2,50 | 2,50 | 2,50 |
| rty fund ... | 9,50 | 4,00 | 5,00 | 2,50 |
| s to staff ... | 3,60 | 2,20 | 1,20 | 96 |
| forward ... | 9,86 | 9,44 | 9,41 | 8,98 |

7. **The Buland Sugar Co., Ltd. and The Raza Sugar Co., Ltd.**

[Both under the managing agency of Messrs. Govan Bros. (Rampur), Ltd.,]

*Table Showing Progress of Production and Earnings*

**Buland Sugar.**

| Year | Total cane crushed | Total sugar manu factured | Recovery | Gross Profit | Net Profit | Dividend |
|---|---|---|---|---|---|---|
| | (In lakhs of Mds) | | % | (Rs. in lakhs). | | % |
| 1935-36 ... | 19.51 | 1.79 | 9.11 | 4.86 | 1.00 | 5 |
| 1936-37 ... | 33 42 | 3.60 | 10 79 | 9.55 | 2.05 | 6 |
| 1937-38 ... | 36.73 | 3 77 | 10.29 | 12 64 | 4 34 | 10+1¼B |
| 1938-39 ... | 17.48 | 1.68 | 9.67 | 6.94 | 2 12 | 10+1¼B |
| 1939-40 ... | 31.27 | 3.18 | 10.175 | 13.68 | 5 16 | 12½ |
| 1940-41 ... | 37.02 | 3.74 | 10 115 | 17.40 | 6.46 | 15+2½B |
| 1941-42 ... | 26.66 | 2 75 | 10.33 | 16 65 | 8.64 | 20+2½B |
| 1942-43 ... | 31.15 | 3 10 | 10.01 | 19.47 | 10.25 | 20+2½B |
| 1943-44 ... | 42.60 | 4.29 | 10 06 | 23 29 | 11.24 | 20+5B |
| 1944-45 ... | 33.24 | 3 48 | 10 547 | 19.21 | 8.63 | 20 |
| **Raza Sugar** | | | | | | |
| 1935-36 .. | 28.95 | 2 62 | 9.06 | .. | 3 82 | 10 |
| 1936-37 ... | 38.10 | 3.71 | 9 75 | 9.18 | 1 79 | 7½ |
| 1937138 ... | 37.31 | 3.62 | 9.70 | 11.90 | 3.94 | 10+2½B |
| 1938-39 ... | 16.68 | 1.56 | 9.39 | 6.86 | 2.23 | 10+2½B |
| 1939-40 ... | 32.51 | 3 10 | 9.54 | 13.27 | 5.26 | 12½ |
| 1940-41 ... | 35.86 | 3 50 | 9 77 | 16 90 | 6.57 | 15+2½B |
| 1941-42 ... | 26.85 | 2.60 | 9 69 | 15.05 | 7.49 | 20+2½B |
| 1942-43 ... | 27.83 | 2.64 | 9 523 | 16 86 | 8.74 | 20+2½B |
| 1943-44 ... | 45.71 | 4.45 | 9.729 | 22.90 | 10 32 | 20+5 B |
| 1944-45 — | 35.87 | 3.67 | 10.26 | 20.09 | 9 14 | 20+5 B |

B. Bonus.

*N. B.*—The net profit shown in the above tables is after meeting all expenses but before providing for depreciation.

*Table Showing Appropriations*

(In thousands of rupees)

| | Depreci-ation | Reserves | Other Funds | Distribu-tion to Sha-reholders | Carry forward |
|---|---|---|---|---|---|
| **Buland** | | | | | |
| 1940-41 ... | 1,09 | 3,00 | 30 | 3 15 | 82 |
| 1941-42 ... | 1,10 | 3,00 | 47 | 4,05 | 71 |
| 1942-43 ... | 1,05 | 3,00 | 62 | 5,40 | 72 |
| 1943-44 ... | 1,00 | 3,00 | 1,05 | 6,00 | 73 |
| 1944-45 ... | 96 | 2,00 | 80 | 4,80 | 63 |
| **Baza** | | | | | |
| 1940-41 ... | 94 | 3,50 | 30 | 2,62 | 74 |
| 1941-42 ... | 92 | 2,00 | 47 | 3,37 | 1,34 |
| 1942 43 ... | ·88 | 2,50 | 62 | 4,50 | 1,40 |
| 1943-44 ... | 85 | 3,50 | 1,05 | 5,00 | 1,15 |
| 1944-45 ... | 83 | 2,50 | 1,05 | 5,00 | 75 |

Note:—There is no Income-Tax in Rampur State where these two companies are situated.

## 8. The Cawnpore Textiles, Ltd and the Elgin Mills Co., Ltd.

(Both under the managing agency of Messrs. Begg, Sutherland & Co., Ltd., Cawnpore)

### Cawnpore Textiles

| Half-year ended | Profit* | Taxation reserve | Depreciation | Reserves | Dividend | | Carry forward |
|---|---|---|---|---|---|---|---|
| | | | | | Amount | % p. a | |
| | Rs. | Rs. | Rs | Rs. | Rs. | | Rs. |
| 30-9-1938† .. | 95 355 | — | 2,01,854 | 1,00,000 | 31,770 | 10 | 26,195 |
| 31-3-1939 .. | 1 25 005 | — | 50,000 | 20,000 | 39,713 | 12½ | 30 237 |
| 30-9-1939 .. | 1,12,870 | 15,000 | 45,000 | — | 46,875 | 12½ | 24,983 |
| 31-3-1940 .. | 1,39,540 | 21,000 | 50,000 | — | 56,250 | 15 | 26,023 |
| 30-9-1940 .. | 1 16,196 | 2,500 | 50,000 | — | 46,875 | 12½ | 27,432 |
| 31-3-1941 .. | 1,88,049 | 31,000 | 50,000 | 30,000 | 56,250 | 15 | 36,981 |
| 30-9-1941 .. | 5,05,908 | 2,64 000 | 75,000 | 50,856 | 93 750 | 25 | 53,034 |
| 31-3-1942 .. | 9,03,231 | 5,82,000 | 1,25,000 | 73,755 | 1,12,500 | 30 | 66,739 |
| 30-9-1942 .. | 13,80 688 | 9,60,000 | 1,00,000 | 99,490 | 1,87,500 | 50 | 94,188 |
| 31-3-1943 .. | 25,26,773 | 18,25,000 | 1 00,000 | 3 98,901 | 1,87,500 | 50‡ | 1,03,310 |
| 30-9-1943 .. | 28,70,615 | 21 50,000 | 1,00 000 | 2,49,686 | 3,00,000 | 40§ | 1,67,989 |
| 31-3-1944 .. | 21,15,922 | 16,35 000 | 1,00 000 | 3,99,514 | 1,12 500 | 15§ | 30,647 |

*Before providing for taxation and depreciation.

†In this year, out of a balance of Rs. 2,51,854 in debenture sinking fund Rs. 1,00,000 was transferred to reserve fund and the balance of Rs. 1,54,854 was credited to depreciation account.

‡Exclusive of a capital bonus of Rs 2 8 0 per share.

§On capital increased by 100 per cent.

### Elgin Mills

| Half year ended | Profit* | Taxation reserve | Depreciation | Reserves | Dividend | | Carry forward |
|---|---|---|---|---|---|---|---|
| | | | | | Amount | % p. a. | |
| | Rs | Rs. | Rs. | Rs. | Rs | | Rs. |
| 30-9-1938 ... | 2,42 388 | 30,000 | 1,00,000 | — | 42,000 | 4 | 21,370 |
| 31-3-1939 ... | 2,96,166 | 40,000 | 1 00,000 | — | 52,500 | 5 | 56,036 |
| 30-9-1939 ... | 3,60,057 | 70,000 | 1,50 000 | — | 63,000 | 6 | 64,093 |
| 31-3-1940 ... | 4,48,837 | 1,10,000 | 1,50,000 | 25 000 | 1,05,000 | 10 | 53,930 |
| 30-9-1940 ... | 6,31 648 | 2,10,000 | 1,75,000 | 47,145 | 1,05,000 | 10 | 79,434 |
| 31-3-1941 ... | 10,05,051 | 4,75,000 | 2,40,000 | 1,00,000 | 1,57,500 | 15 | 82,985 |
| 30-9-1941 ... | 18,96,925 | 11,30,000 | 2,50,000 | 1,49,910 | 2,10,000 | 20 | 1,71,001 |
| 31-3-1942 .. | 21,19 851 | 12,50,000 | 2,50,000 | 1,99,902 | 3,15,000 | 30 | 1,91,950 |
| 30-9-1942 ... | 31,48,520 | 23,00,000 | 2,00 000 | 1,99,787 | 3,67,500 | 35 | 2,04,182 |
| 31-3-1943 ... | 61,69,173 | 48,32,228 | 2,50,000 | 2,99,787 | 6,82,500 | 65 | 2,39,652 |
| 30-9-1943 .. | 71,48,644 | 54,00,000 | 2 50,000 | 4,87,776 | 8,40,000 | 80 | 3,41,521 |
| 31-3-1944 .. | 57,41 818 | 45,00 000 | 2,50 000 | 8,49,945 | 3,15,000 | 30 | 1,13 894 |

*Before providing for taxation and depreciation but after meeting all expenses including Managing Agents' commission, auditors' and directors' fees etc.

*N B* —Referring to the increase in transfer to reserves of both the Companies, the Directors in their report to the shareholders state · "The large transfer to general reserve is necessitated in order to meet the payment of compulsory deposit"

9. **Messrs. Andrew Yule-Jute Group.**

(Consisting of the Albion Jute Mills Co., Ltd., the Caledonian Jute Mills Co., Ltd., the Cheviot Mills Co., Ltd., the Delta Jute Mills Co., Ltd., the Lothian Jute Mills Co., Ltd., and the Orient Jute Mills Co., Ltd.)

The following comparative table shows more clearly how the results for the half year under review compared with those for the previous half-year, as also the corresponding half-year of 1943:—

(In thousands of Rupees)

| Half-year ended | Sales | Gross profit | Depreciation | Taxation reserve | Net profit | *Dividend (Ordinary) | Carry forward |
|---|---|---|---|---|---|---|---|
| **Albion Jute** | | | | | | | |
| 31- 5-'44† ... | 25,99 | 2,50 | ... | 58 | 91 | 6% | 37 |
| 31-10-'43 ... | 15,15 | −3,70 | ... | −3,74 | −42 | 6% | 24 |
| 30- 4-'43 ... | 19,81 | 1,12 | ... | 20 | 56 | 8% | 34 |
| **Caledonian** | | | | | | | |
| 31- 5-'44 ... | 2,78 | 2,62 | 25 | 75 | 74 | 15% | 31 |
| 30-11-'43 ... | 21,47 | −3,55 | 50 | −3,70 | −90 | 15% | 33 |
| 31- 5-'43 ... | 32,31 | 4,89 | 50 | 2,65 | 1,19 | 20% | 51 |
| **Cheviot** | | | | | | | |
| 31- 5-'44 ... | 39,81 | 7,69 | 50 | 4,60 | 1,52 | 12% | 62 |
| 30-11-'43 ... | 29,28 | 2,50 | 50 | 45 | 74 | 8% | 40 |
| 31- 5-'43 ... | 30,41 | 6,05 | 50 | 3,65 | 1,22 | 12% | 65 |
| **Delta Jute** | | | | | | | |
| 31- 5-'44 ... | 33,63 | 4,18 | ... | 2,00 | 1,39 | 20% | 67 |
| 30-11-'43 ... | 26,83 | −2,55 | ... | −3,70 | 65 | 20% | 83 |
| 31- 5-'43 ... | 42,97 | 7,74 | ... | 5,15 | 1,87 | 30% | 123 |
| **Lothian Jute** | | | | | | | |
| 31- 5-'44 ... | 27,15 | 2,24 | 50 | 40 | 50 | 6% | 29 |
| 30-11-'43 ... | 21,18 | −2,90 | 50 | −3,70 | −34 | 6% | 44 |
| 31- 5-'43 ... | 29,03 | 4,14 | 50 | 2,25 | 76 | 8% | 44 |
| **Orient Jute** | | | | | | | |
| 31- 5-'44 ... | 27,99 | 2,54 | 40 | 60 | 68 | 7% | 67 |
| 30-11-'43 ... | 20,72 | −2,34 | 40 | −3,18 | −20 | 7% | 86 |
| 31- 5-'43 ... | 28,99 | 4,44 | 40 | 2,60 | 95 | 10% | 119 |

*Dividend per cent. per annum.

†The results cover the seven month period ended 31st May, 1944.

While the table is self explanatory in many respects, some comment is necessary in regard to the transfers from taxation reserves relating to the half year ended 30th November, 1943. The transfer of Rs. 3.74 lakhs in the case of the Albion Jute is made up of Rs. 3,50 lakhs, being estimated tax refundable, and about Rs. 24,000 representing excess provision for taxation. But for these transfers, the loss on the

net profit account would have been considerable. Even these transfers were not sufficient to enable payment of dividends, and it was found necessary to draw from dividend equalisation reserve to the extent of rupees one lakh. The dividends for the period under review however, have been fully earned and there have been no transfers from the reserve funds.

In the case of Caledonian Jute, the transfer of Rs. 3.70 lakhs from taxation reserve, as shown in the table, includes Rs. 2.20 lakhs excess provision for taxation in previous years and Rs. 1.50 lakhs being estimated tax refundable. Besides these transfers, the Directors had to draw Rs. 1.75 lakhs from dividend equalisation reserve in order to pay even the reduced dividend. In the half-year under review, although there have been no withdrawals from taxation reserve, it has been found necessary to make a small draft of only Rs 25,000 on dividend equalisation reserve so that dividend could be maintained at 15 per cent, per annum.

In the case of the Delta, the entire transfer of Rs. 3.70 lakhs consisted of excess provision for taxation in previous years. The Directors had also to draw Rs. 50,000 from dividend equalisation reserve. In the half-year under review, however, no transfers of this nature have been found necessary. Similarly, both the Lothian and the Orient Jutes had to make inroads into their reserves in addition to the withdrawals from taxation reserves. The former took rupees one lakh from dividend equalisation reserve and the latter Rs, 75,000 from general reserve. But, during the latest half-year, the need for such transfers has been obviated.

It will be noted from the foregoing that the Cheviot Jute stands out in a class by itself, in that it is the only company in the group which did not suffer any loss even in so difficult a half-year as the one ended November, 1943. This is chiefly due to the fact that the mill is being driven by electricity and as such its working is not so susceptible to periodical shortages of coal as that of steam power-driven mills.

## THE TATA POWER COMPANY, LIMITED.

### COMPARATIVE STATEMENT OF SALES AND FINANCIAL RESULTS.

| Item | 1939—40 | 1940—41 | 1941—42 | 1942—43 | 1943—44 | 1944—45 |
|---|---|---|---|---|---|---|
| Power Sales—Millions of Units — | 300·21 | 382·85 | 425·99 | 456·80 | 511·96 | 534 39 |
| | Rs. | Rs. | Rs | Rs. | Rs. | Rs. |
| Revenue from Power Sales ... .. | 75,19,893 | 81,71,192 | 90,12,095 | 93,69 472 | 1,01,62,788 | 1,07,32,587 |
| .. from Other Sources ... | 3,69,290 | 3,15,578 | 1.26,730 | 1,49,406 | 2 02,361 | 2,05,080 |
| Total Gross Revenue | 78,89,183 | 84,86,770 | 91,38,825 | 95,18,878 | 1,03,65,149 | 1,09,37,667 |
| Net Profit before providing for Depreciation and Taxes) ... .. | 31,29,064 | 54,43,261 | 58,78,027 | 58,68,316 | 69 05,237 | 62,65,286 |
| *Deduct :* Depreciation ... ... | 12,78,000 | 12,78,000 | 12,77,000 | 12,77,000 | 10,00,000 | 9,00,000 |
| Provision for Taxation ... | 5,86 918 | 11,01,304 | 14,27,000 | 17,30,000 | 26,20,000 | 25,78,000 |
| Balance ... | 32,64,146 | 30,63,957 | 31,74,027 | 28,61,316 | 32,85,237 | 27,87,286 |
| *Add ;* Income tax recovered from Pref. Dividends ... ... | 1,01,918 | 1,06,167 | 1,44,386 | 1,61,372 | 1,76,658 | 1,88 550 |
| Amount carried forward from previous year ... ... | 4 81,840 | 5,42,788 | 1,85,159 | 2,89,445 | 1,14,592 | 1,48,921 |
| Transferred from General Reserve ... ... | ... | — | .. | 2,00,000 | ... | 50,000 |
| Total ... | 38,47,904 | 37,12,912 | 35 03,572 | 35,12,133 | 35,76,487 | 31,74,757 |
| APPROPRIATIONS :— | | | | | | |
| Reserve for Taxation—Supplementary | ... | 3,34,863 | 19,346 | 2,49,000 | 2 46,000 | 1,60,000 |
| Bonus to Staff ... . | 36,000 | 36,500 | 37,000 | 36.000 | 72,000 | 72,000 |
| Debenture Expenses Written Off ... | ... | 62,180 | 62,979 | .. | ... | ... |
| Reserve for Special Repairs ... | 8,337 | 1,665 | 2,257 | 19,996 | 17 021 | ... |
| General Reserve ... ... | 4,00,000 | ... | ... | ... | ... | ... |
| Total ... | 4 44 337 | 4,35,208 | 1,21,582 | 3,04,996 | 3,30,021 | 2,32,000 |
| Balance available for distribution ... | 34,03,567 | 32,77,704 | 33,81,990 | 32 07,137 | 32,41,466 | 29,42,757 |
| Total Dividend Paid—Preference Shares | 6,52,275 | 6,52,275 | 6,52 275 | 6,52,275 | 6,52,275 | 6,52,275 |
| " " —Ordinary Shares ... | 22,08,504 | 24,40,270 | 24,40,270 | 24,40,270 | 24,40 270 | 22,65,965 |
| Percent Dividend .. ... | 6¼ | 7 | 7 | 7 | 7 | 6¼ |
| Balance carried forward ... ... | 5,42,788 | 1,85 159 | 2,89.445 | 1,14 592 | 1.48,921 | 24,517 |

### Interpretation of the analysis of Working.

Since the publication of an annual profit and loss account is made compulsory for all public companies, it means that the importance of the profit and loss account for the purpose of assessing the value of a company's business has been duly recognised by law. Generally speaking, the only thing that gives business assets any value is the annual profit that can be made by their use—either present profit or an anticipated profit. The value of an asset or a group of assets at any particular time may well be a matter of opinion, but the profit earned in a particular period is largely a matter of fact.

Many people are apt to pay too much attention to a company's balance sheet and too little attention to its profit and loss account. It is true that a company's balance sheet exhibits a position which is the result of transactions that have taken place during the whole of its life whereas the profit and loss account only shows what the profits are for the last year; and it may be true also that, owing to the special circumstances, the profits of that company for that particular year are abnormally high or abnormally low and therefore afford little guide as to future probabilities. But a comparison of the results with those shown by the profit and loss accounts of preceding years, coupled with such information as is afforded by the directors' reports and the chairman's speeches at the annual meetings furnishes, as a general rule, a better guide to the approximate value of a business than does the balance sheet.

When considering the affairs of a company from its published accounts, we cannot foretell the future, but we can guess at it successfully from a scientific study of its past.

After a comparative analysis of the results of a company's working has been prepared in the manner explained above, the following points must be examined :—

1. **Sales.** The sales are the life-blood of every business. If the sales of a business are declining and if no steps are taken to arrest their decline, the very existence of the business may be in danger.

Note the trend of sales over the period and their effect on the figure of working or gross profit, because an improvement in sales may or may not be reflected in gross profit. Ascertain the relation between the sale proceeds, the cost of production and establishment charges and the figure of gross profit. If the sales, expenses and the gross profit have all moved in an upward direction, then there must have been an increase in selling prices at the cost of consumers; but if the sales and expenses have both increased but the gross profit remains unchanged, the margin of profit must have remained unchanged. Where there is a marked rise in sales but the profit is lower, this must be due to a sharp increase in the cost of production and establishment charges. If the entire increase in sale proceeds is reflected in the gross profit without an increase in selling prices, this can be possible only when there is strict control over expenditure.

2. **Stocks.** Examine the trend of stocks, which may be of stores, raw materials and finished goods. Mounting stocks indicate slow trade and unnecessary lock-up of capital. A substantial rise in

stocks may be accounted for by a decrease in sales and also by the larger purchases made to safeguard the future position of the company. During the recent war period when stores and raw materials have been difficult to obtain, there has been a common tendency on the part of many companies to carry large stocks of stores and raw materials

3. **Other Income.** Ascertain the various sources from which the company has derived its income with special reference to any capital or extraneous profits, and see if there is any source which will not be available in future. It is just possible that a substantial portion of a company's earnings may have been derived from gilt-edged investments, and if the greater part of the investments has been recently sold in order to provide additional working capital, the future income from investments would be considerably reduced.

4. **Expenditure.** One of the killing diseases of a business is increasing expenditure not accompanied by a corresponding expansion in turnover. By comparing the percentage of expenditure to sales for a number of years it is possible to ascertain whether the expenses of a company are unduly increasing.

5. **Percentage of Profit.** In order to ascertain the correct relation of gross profit to sales it is essential that its percentage to sales should be worked out. If the absolute figures of gross profit are compared from year to year, the comparison may give a false idea of the company's progress. Suppose the sales of a company for 1943, 1944 and 1945 are Rs. 10,00,000, Rs. 12,00,000 and Rs 16,00,000 and the gross profit Rs. 1,20,000, Rs. 1,50,000 and Rs. 1,60,000 respectively. If we compare the absolute figures of gross profit the year 1945 appears to be the best because the gross profit for that year is the highest. But that is certainly not the case. The percentages of gross profit to sales for the three years are 12%, 12½% and 10%, which means that 1944 has given the best result.

6. **Profits vis-a-vis Capital Employed.** Examine the trend of the company's earnings—whether improving, steady or declining. Earnings are, however, meaningless unless they are related to the capital employed during the period in which they have accrued. Judged by earnings alone a company may appear decidedly progressive; but the examination of the accounts for several years may show that every rupee of new capital put into the business is obtaining a decreasing return. Therefore it is essential to ascertain and compare the percentage of earnings on the effective capital employed in the business.

This point is very aptly illustrated in the following extract from the Chairman's speech delivered at the annual general meeting of the Bombay Telephone Co., Ltd. held in March 1939:—

"From time to time criticism is offered of dividends paid by companies, more particularly when those companies are operating public utility undertakings.

"It is never enough merely to consider the amount or percentage of the dividend itself. Before any useful view can be formed on the subject it is necessary to examine the position and ascertain what

is the real amount of capital employed and what is the real return on that.

"In the case of this Company, until the very end of last year the subscribed Share Capital was just over Rs. 1 crore but in addition to that the Shareholders had left in the business a sum of approximately another crore. In the main that sum was put aside as provision for wasting assets but as it has not yet been required for that purpose it has been used to pay for new additional assets necessitated by the expansion of the Company's undertaking. The matter perhaps becomes plainer if I say that these funds could have been invested outside the Company's business and in that event we may assume that they would have been bringing in a return somewhere in the neighbourhood of 3 per cent. per annum. Had that course been followed, in order to pay for addditional assets from time to time it would have been necessary either to borrow a sum of approximately Rs. 1 crore or to increase the Share Capital, but there certainly seems to be no point in investing large sums of money at a lower rate of interest than would have to be paid to borrow the same amount.

"You will appreciate that this means that though the dividend paid on the Subscribed Capital is 8 per cent. the approximate return on the Capital employed is much nearer to 4 per cent a return which is by no means high when you remember that one of the essential points to bear in mind in conducting the affairs of an undertaking of this nature is the great importance of being in a position to raise additional fund from time to time as they may be required in connexion with the expansion which must normally be expected to take place. For that purpose it is essential in the interests of the public as well as the Shareholders to have a sound Balance Sheet and show a reasonable return on the Capital employed, whether that Capital be Share Capital, borrowed money, reserves or other finance, and the scale of charges to subscribers has to be framed accordingly,"

7. **Provision for Depreciation and Taxation.** The importance of making adequate provision for the depreciation of block and for the taxation liability has already been discussed in the preceding pages. Find out whether the provision for depreciation and taxation is adequate and in doing so take into consideration the various factors mentioned on pages 150, 151, 152. In recent years the question of depreciation and taxation has assumed special significance in company finance.

8. **Transfers to Reserves.** The conservation of the resources of a company by means of transferring adequate amounts to the various reserves is very desirable in view of the post-war difficulties with which all companies are now confronted.

If the block account of a company has already been depreciated to a low level and if the existing reserves are sufficient, any further allocation for depreciation and reserves on the same scale is open to objection. This means that a substantial portion of the profits is 'ploughed back' or diverted to other channels than that of shareholders. Such a financial policy is, of course, very sound, but is certainly not correct On the other hand, the policy of frittering away the huge profits of prosperity by declaring extravagant dividends, without making provision for times of adversity or for future growth, is to be condemned. What is needed is a sense of proportion. Both these

extremes—the ploughing back of a substantial portion of the earnings and the up to the-hilt distribution—are to be avoided. While it is necessary to make adequate provision for depreciation and reserves, it is equally desirable that the shareholders who have supplied the capital should not be deprived of their just dues,

9. **Dividend Record** The essentials of a sound financial policy governing the distribution of a company's profits have been thoroughly examined in an earlier chapter. See whether the dividends declared and the amount left to be carried forward conform to a sound financial policy. Note also whether the dividends distributed have all been earned or whether a draft has been made upon the past profits It is obvious that a steady dividend policy is desirable both in the interest of the company itself and that of the shareholders.

10. **Economic Environment.** While examining the figures contained in the comparative statement of the company's working, it is equally important to consider the economic environment of the company. The directors' report and the chairman's speech will certainly contain some information relating to the company's economic position The economic environment of a company can be judged by answers to the following questions :—Is the company's business well situated as regards the supply of raw materials, labour, motive power and markets ? Is the plant and equipment adequate, up-to-date and kept in good repair ? Is the output commensurate with the equipment and is it of a quality which can find a ready market ? Is labour supply satisfactory or is there any difficulty in securing the type of labour required ; is labour well paid and contented ? Are there any special advantages enjoyed by the company, such as economies of coordinated management, means available for the disposal of bye-products, tariff protection, market assurance, or rationalisation ? Are there any particular drawbacks such as unhealthy competition, lack of expert technical assistance, scarcity of raw materials, shortage of labour or coal, imposition of excise duty, etc. ? Are there any political or fiscal influences bearing directly on the business of the company ?

By carefully examining all these factors one can easily measure the progress of a company.

### II. The Company's Financial Position.

The balance sheet of a company is intended to exhibit its financial position ; and for the protection of the investing public its contents are prescribed by law. However ably a balance sheet may have been drawn up, it has always certain limitations. These are :—

1. A balance sheet is not a valuation statement The various assets appearing therein are valued according to certain recognised accountancy principles. The floating assets are valued on the basis of cost or market price, whichever is less : and as the object is to convert all floating assets into cash at the earliest possible opportunity, no profit is anticipated before they are actually sold. The fixed assets, on the other hand, appear in the balance sheet at cost less reasonable depreciation.

The danger to be guarded against is that those who try to estimate the value of a business from its balance sheet may not understand the accounting mind and may therefore asses the worth of such fixed assets at the value stated instead of regarding it as merely a 'going concern' or token figure.

2. Unless a balance sheet is read in conjunction with the profit and loss account, it fails to disclose the earning capacity of a business; and it is the earning capacity alone which gives a real indication of the total value of a business as a going concern.

3. Some people think that there should be no secret reserves and that a balance sheet which does not disclose the existence of all reserves does not exhibit a true and correct view of the state of the company's affairs But it must be remembered that if all secret reserves were shown on the balance sheet a number of practical difficulties would arise.

Whatever may be the limitations of as balance sheet and however difficult it may be to read and understand, it is in fact the most important document that comes into the hands of a shareholder. It is far more significant than a dividend cheque. If the balance sheet tells an unsatisfactory tale, the dividend cheque will eventually cease altogether.

In order to ascertain the financial position of a company, its balance sheet must be carefully examined. But when studying a published balance sheet (containing a mass of information and sometimes running to several pages), it is important to remember that unless it is entirely broken into pieces and rebuilt, it will tell the reader nothing except that its two sides are equal. It should, therefore, be rearranged in the form of a synopsis, so that the financial position of the company may stand out at a glance. The following form is suggested for this purpose :—

Synopsis of Balance Sheet as on ..... .. ......

| | Rs. | | Rs. |
|---|---|---|---|
| Share Capital ... | | Gross Block ... | |
| Debenture ... | | *Less* Depreciation ... | |
| Reserves ... | | Net Block ... | |
| Taxation Liability ... | | Stores ... | |
| Other Liabilities ... | | Stocks ... | |
| Carry-forward ... | | Book Debts, Advances Deposits ... | |
| | | Investments ... | |
| | | Cash Balances ... | |

If it is desired to have a comparative synopsis of the balance sheets for several years, additional columns will be provided on either side. The amount of proposed dividends (unless already given effect to in the published accounts) must be included in the item of other liabilities. The details of the share capital may be given as a footnote.

A few specimen synopses of balance sheets are given below, the first two being taken from the "Indian Finance" and the rest from the "Commerce".

## 1. The Rellance Jute Mills Cn., Ltd.

Anthorised, Issned and Snbscribed Capital—Rs. 36,50,000 in 1,65,000, Ordinary of Rs. 10 and 20,000, 7 per cent Cnm. Pref. shares of Rs. 100, both fully paid up

Synopsis of the balance sheet as at 30th September, 1943.

| *Liabilities* | Rs. | *Assets* | |
|---|---|---|---|
| Capital paid up | 36,50,000 | Gross Block ... | 89,19,489 |
| Reserves and other funds ... | 52,03,122 | Depreciation ... | 49,94,411 |
| Current debts including taxation ... | 26,67,112 | Block (net) ... | 39,25,078 |
| Carry forward ... | 64,071 | Stores ... | 10,53,562 |
| | | Stock-in-Trade ... | 36,50,018 |
| | | Outstandings ... | 13,83,513 |
| | | Investments ... | 13,92,322 |
| | | Cash balances ... | 1,79,812 |
| Total ... | 1,15,84,305 | Total ... | 1,15,84,305 |
| | | Total Liqnid Assets | 76,59,227 |

## 2. The Titaghur Paper Mills Co., Ltd.

Anthorised, Issued and Snbscribed Capital—Rs. 65,89 000 divided in 11,500. 8 per cent First Cumnlative Preference shares of Rs. 100 each, 15 000, 5 per cent Second Cumulative Preference shares of Rs. 100 each, 1,75,000 Pref. ordy. shares of Rs. 2-8 each, 3,50,000 "A" Ordy. shares of Rs. 5 each, and 3,50,300 "B" Ordy. shares of Rs. 5 each, and all fully paid up.

Synopsis of Balance Sheet as at 30-9 -1944.

| *Liabilities.* | Rs. | *Assets.* | Rs |
|---|---|---|---|
| Capital P'up ... | 65,89,000 | Gross Block ... | 2,64,52,853 |
| $4\frac{1}{2}$% Debentures ... | 25,00,000 | Depreciation ... | 2,02,04,203 |
| Reserve and other funds ... | 73,34,194 | Block (net) ... | 62,48,650 |
| Current liabilities including taxation | 1 50,67,983 | Stock ... | 63,70,311 |
| Carry-forward ... | 5,01,684 | Outstandings ... | 89,55,223 |
| | | Investments ... | 68,29,583 |
| | | EPT Deposits ... | 34,08,631 |
| | | Cash ... | 1,80,463 |
| *Total* | *3,19,92,861* | *Total* | *3,19,92,861* |
| | | Liq. Assets | 2,57,44,211 |

3.

**The Hindusthan Sugar Mills, Ltd.,**

Synopsis of Balance Sheets.

| | As at 30-6-1944 | As at 30-6-1941 |
|---|---|---|
| **Liabilities.** | Rs. | Rs. |
| Capital ... ... | 15,00,000 | 15,00 000 |
| Reserve fund ... ... | 15,00 000 | 1,15,000 |
| Other funds and surpluses ... | 22,927 | 13,232 |
| Reserve for taxation ... ... | 8,40,519 | 92,652 |
| Liabilities* ... ... | 58,83,076 | 33,89 261 |
| **Assets.** | | |
| Gross block ... ... | 21,28,783 | 30,31,326 |
| *Less* depreciation ... ... | 17,50,000 | 13 00,000 |
| Net Block ... ... | 13,78,783 | 17,31,326 |
| Stocks and stores ... .. | 72,71,354 | 31,59,517 |
| Book debts, etc. ... ... | 5,40,466 | 1,90,684 |
| Cash ... | 55,919 | 28,618 |
| Total .. | 92,46,522 | 51,10 145 |

* Including such in respect of the proposed dividend.

4

**The Belapur Co., Ltd.,**

Synopsis of Balance Sheets.

| | As at 30th September | | | |
|---|---|---|---|---|
| | 1944 | 1943 | 1942 | 1941 |
| **Liabilities.** | Rs. | Rs | Rs. | Rs. |
| Capital ... | 37 59,800 | 37,59 800 | 37,59,300 | 37,59,800 |
| Reserve, other funds and surpluses* ... | 17,54,501 | 15,19,795 | 11,98,160 | 10,04,768 |
| Reserve for taxes ... | 10,25,280 | 7,35,209 | 6,88 460 | 8,27,643 |
| Liabilities† ... | 12,31,732 | 10,76 331 | 9,38,492 | 11 97,887 |
| **Assets** | | | | |
| Block ... | 31,08,345 | 33,75,563 | 36,14,392 | 35,40,207 |
| Stores, etc. . . | 7,41,007 | 5 74,409 | 6,22,050 | 4,71,650 |
| Stocks .. | 8,24,684 | 4,40,757 | 2,60,421 | 14,010 |
| Crop in-progress ... | 17,33,095 | 17,72,124 | 12,34,534 | 11,72,507 |
| Book debts and advances .. | 1,85 890 | 1,22,140 | 70,568 | 28,6,284 |
| Investments . | 8,11,153 | 12,546 | 2,05,885 | 11,78,204 |
| Cash ... | 3,67,138 | 7,93,596 | 5,77,062 | 1,27,236 |
| Total ... | 77,71,313 | 70,91,135 | 65,84,912 | 67,90,098 |

* Include the carry forward.

† Include the liabilities in respect of the dividends proposed for the respective years.

5. **The Kesoram Cotton Mills, Ltd.**

As regards the finances of the Company, the following comparative table will be read with interest :

| | As at 30-9-'43 | As at 30-9-'42 | As at 30-9-'41 |
|---|---|---|---|
| **Liabilities** | Rs. | Rs. | Rs. |
| Capital ... | 40,00,000 | 35,00 000 | 35,00,000 |
| Reserve funds ... | 13,01,366 | 17,97,293 | 16,11,955 |
| Provision for taxation .. | 56,40,000 | 10,50,000 | 4,00,000 |
| Liabilities† ... | 30,15,984 | 19,34,374 | 39,37,208 |
| Undistributed surplus profit ... | 3,01,371 | 11,82,071* | 46,192 |
| **Assets** | | | |
| Block (net) ... | 24,00,000 | 30,00,000 | 36,35,867 |
| Stores ... | 7,63,061 | 3,57,324 | 3,51,099 |
| Stocks ... | 39,22,513 | 35,83 864 | 23,13,941 |
| Debts and advances ... | 33,66,633 | 10,06,958 | 30,74,407 |
| Investments ... | 17,53,751 | 13,60,996 | 23,227 |
| Cash ... | 20,52,763 | 1,44,597 | 96,814 |
| Balance-sheet total ... | 1,42,58,721 | 94,63,739 | 94,93,355 |

*Subject to provision for taxation.
†Include amount payable by way of dividend.

6. **The Bank of India, Ltd.**

Synopsis of Balance Sheets.

(In lakhs of rupees)

| | As at 31st December | | | | |
|---|---|---|---|---|---|
| | 1943 | 1942 | 1941 | 1940 | 1939 |
| Deposits— | Rs. | Rs. | Rs | Rs. | Rs. |
| Fixed ... .. | 9 19 | 6,71 | 7,35 | 8.47 | 8,17 |
| Current ... ... | 45 94 | 30,11 | 18,50 | 13,80 | 10,42 |
| Advances ... | 13,51 | 9,38 | 11,05 | 7,52 | 9 97 |
| Property ... .. | 4 | 8 | 13 | 15 | 15 |
| Investments in Government securities and equities ... . | 18,59 | 8,34 | 7,95 | 5,41 | 4,96 |
| Treasury bills ... ... | 12,96 | 12,06 | 3,73 | 5,36 | 2,14 |
| Cash balances .. ... | 12 70 | 9,58 | 5,41 | 6,15 | 3,73 |
| Capital ... ... | 1,00 | 1,00 | 1,00 | 1,00 | 1,00 |
| Reserves ... ... | 1,24 | 1,21 | 1,19 | 1,16 | 1,14 |

### Interpretation of the Summarised Balance Sheet

In order to ascertain the financial position of a company from the synopsis of its balance sheet, the following points should be considered :—

1. **Capital Structure.** Note the amount and the form of share capital. If there are shares of more than one class, what are the

dividend arrangements between them, and what are the special rights attached to them? This information will not be available from the published accounts, but will have to be obtained from the company's articles of association. In the case of companies whose shares are quoted on the stock exchanges, full information regarding the capital structure may, however, be obtained from the well known reference books on the subject, such as the *"Investor's India Year Book"* by Messrs. Place, Siddons & Gough, Stock Brokers of Calcutta or the *"Bombay Stock Exchange Year Book"* by Mr. M. C. Mehta, Share Broker, Bombay, or a similar book by Messrs. Kothari & Sons, Share Brokers of Madras.

Taking the size of the company into consideration, is the amount of its share capital heavy, moderate or inadequate? In other words, is the company overcapitalised or undercapitalised?

Whether a company is overcapitalised can be judged by reference to its earning capacity. If the net profits, after making provision for all prior charges, are sufficient to ensure a reasonable return on the issued capital, having regard to the nature of the business and the risks involved, it cannot be said that the company is suffering from overcapitalisation. On the other hand, a company is undercapitalised if there is an undue proportion of borrowed money or of trade creditors. This is a gradual process brought about by a continuous expenditure on capital assets in excess of the profits retained in the business or by an expansion of business requiring larger stocks and possibly a greater volume of outstanding debtors than was contemplated when the original capital was fixed. The importance to the shareholders of such a state of affairs is that it cannot be regarded as permanent, and it may lead to the raising of further permanent capital on terms which may or may not be advantageous to existing shareholders.

Ascertain also the gear ratio, i. e the proportion between the fixed interest capital (preference share capital and debentures) and the ordinary share capital. It must be recognised that high geard equity shares are very speculative, and high gearing is bad from the point of view of the company and the perference shareholders and debenture-holders as well.

A very fine article by Mr. P. Chandra, M A., late of the U. P. Civil Service, on 'The Capital Structure of Public Companies' appeared in the *"Commerce"* of 28th November and 4th December 1944; and it is reproduced in the Appendix with due acknowledgment to the author and the *"Commerce"*.

2. **Debentures.** Note the amount of debentures and the terms on which they have been issued. Full information relating to the debentures will be found either in articles of association or in one of the reference books stated above. Are the debentures a burden on the earnings of the company, having regard to their amount and the rate of interest they carry? What assets have been mortgaged as security? When were the debentures issued—for block requirements or for working capital? When are they redeemable? Does a sinking fund exist for their redemption? If so, is it represented by earmarked investments?

3. **Reserves.** The various types of reserves met with in Indian published accounts have been mentioned in an earlier chapter. The

reserves are in fact funds given by the shareholders upon which they are not entitled to any return. Compare the amount of reserves with paid-up capital. The higher the reserves the stronger the financial position of the company, because they provide working capital or current finance for stocks and stores without any cost by way of interest or dividend. Have the reserves been expended on the acquisition of block or are they held in liquid form?

4. **Liabilities.** These consist of secured and unsecured loans and current liabilities for goods purchased, expenses proposed dividends, etc. Bank loans and other temporary borrowing is generally resorted to for the purpose of financing stocks and stores. In a company whose finances are in a healthy condition such loans are usually small. Note the trend of liabilities. Are they increasing? Examine also the relation between liabilities and current assets, more particularly the relation between immediate liabilities and liquid resources. The liabilities may have considerably increased; but if the floating assets have also increased more than proportionately, there need be no cause for worry.

5. **Block Account.** Compare the book value of the block with the company's share capital and debentures. As a matter of sound financial policy, the fixed finance of the company should be more than sufficient to cover block requirements. The financing of a part of the block out of short-term loans is undesirable. See that the block is adequately depreciated having regard to the age of the various fixed assets. The question of replacement of worn-out machinery and plant should also be looked into. The necessary information regarding these questions will be found in the directors' report and the chairman's speech.

6. **Current Assets.** These consist of stores, stocks book-debts, advances, Investment, deposits and cash balances. Does the company carry an adequate stock of stores? Are the stocks of raw meterials and finished goods properly valued? Does the stock-in-trade tend to Increase from year to year? Have stores and stocks been financed out of reserves or by means of borrowed money? Compare the amount of book debts with trade creditors. With regard to investments, what are they—gilt—edge, debentures or industrial securities? How have they been valued? Is there any depreciation or appreciation? Are they a source of strength to the company or are they a cause of weakness?

What proportion do current assets bear to the total assets of the company? The greater the proportion of the current assets the stronger the finances of the company. The total of the assets may also be compared from year to year. A substantial increase in the total assets indicates an expansion in the activities of the company.

Examine the composition of the current assets. What proportion of the current assets is in the form of liquid assets, i. e, investments and cash and what is the nature of the investments?

Note the amount of the E. P. T. compulsory deposits and find out whether any credit has been taken for the post-war refund of the E.P.T. paid and for the interest receivable from Government on such deposits. In the case of all good companies it has been the practice not to include any such credits in the profit and loss account and the balance sheet.

7. **Ways and Means Position.** What is the ways and means position of the company? That is to say, how do its cash and bank balances

stand *vis a vis* its immediate liabilities in the shape of taxation and proposed dividends ? In recent years the taxation liability of companies has assumed special significance

8. **Surplus Liquid Assets** Ascertain the amount of surplus liquid assets by deducting current liabilities from the current assets. The higher this surplus the stronger the financial position of the campany. One of the important uses of a balance sheet is the disclosure of the strength or the weakness of what is commonly known as the liquid position of a company, that is to say, the position in regard to its floating assets and its floating liabilities. Has the company sufficient floating capital for its ordinary needs ? Has it a surplus of floating capital over and above its ordinary needs which would be available to make good losses which may arise in unforeseen circumstances ? Has the business surplus floating capital which could be utilised in meeting any capital expenditure which may be necessary for the continued extension of its activities ?

9. **Management** The capital of a company is supplied by those who take no participation in its control and who have no knowledge of the business, and a new element, namely 'management' has been introduced. On the ability of that management depends both the value of the goodwill and the value of the fixed assets for the mechanisation of industry has made the value of the works and plant more and more subject to the earning capacity of the business. The worth of the fixed assets, therefore, varies with the value of the management, and the latter is an asset of no tangible or permanent value capable of appraisement, except in a negative way, in a balance sheet.

You may teach rationalisation of Industry or you may preach nationalisation of industry as the solution of our economic problems ; you may introduce artificial aids of a temporary nature such as State-aided finance, tariffs, and subsidies ; you may appoint Royal Commissions, Committees, and Trade Federations, but, in the end, the value of a business depends on the men who run it

> Though your Balance Sheet's a model of what Balance Sheets should be ;
> Typed and ruled with great precision in a type that all can see ;
> Though the grouping of the assets is commendable and clear,
> And the details which are given more than usually appear ;
> Though investments have been valued at the sale price of the day,
> And the auditors' certificate shows everything O. K. ;
> One asset is omitted—and its worth I want to know ;
> That asset is the value of the men who run the show.
> Sir Mark Webster Jenkinson : *The Value of a Balance Sheet.*

In appraising the value of a company's business the factor of management is, therefore, of the utmost importance ; and it is more so in a country like India where there is still dearth of industrial leadership. Information should be obtained from whatever sources available in order to judge whether the management of the company is experienced efficient, economical and honest ; whether the company enjoys any economies of coordinated management by being one of

several similar units under the same control, whether the management is capable of replacement without disturbing the continuity of the business or whether it is a 'one man show', the disappearance of the chief actor ringing down the curtain.

### III. The Company's Prospects.

When the published accounts of a company have been examined and its working results and its financial position ascertained, it is equally important to know something about its future prospects. For this purpose it is necessary that some knowledge of the industry in which the company is engaged must be obtained from study of one or more financial newspapers and that a reference should be made to its directors' report and its chairman's speech delivered at the annual general meeting. The directors' report and the chairman's speech of a well conducted company will certainly contain some information relating to the company's future prospects.

The following extracts taken from chairman's speeches delivered at company meetings illustrate the kind of information that is usually given regarding a company's future prospects :—

1. **The Associated Cement Companies, Ltd.** Annual Meeting held in January 1945.

There are several factors which incline your Board to view the future with a certain measure of assurance. Cement will be in the forefront of the industries whose rational development is regarded as essential in the national interests. Large-scale projects for roads, irrigation, public works and the like will be undertaken in the immediate postwar period, and the needs of devastated areas in neighbouring countries will call for a greater export demand, at least until such time as their own cement factories are in a position to supply their requirements. As I have said, this Company is fully prepared for a considerable expansion of its capacity, based on plans which have been carefully worked out. Its plant, its technical personnel and its financial resources all afford an assurance of the maintenance of the important position it holds in the industry, and the long term prospects may therefore be regarded with quite confidence. It is timely, nevertheless, to sound a note of warning against haphazard and ill-conceived expansion, such as was allowed to occur in the decade following the conclusion of the first World War, when investors in the industry had to suffer considerable losses. It is to be hoped that history will not be permitted to repeat itself, and that only the most carefully prepared schemes for industrial expansion, backed by the knowledge, the resources and the ability to implement them will receive consideration and support.

I wish I could say something definite about the prospects for the current year. As is the case with other industries, coal is our greatest headache, and until the situation with regard to this essential raw material and in respect of transport improves, it is not possible to speak with any assurance about the present position. For your information, I may add that our contract with the Government of India, who have been for a long time our largest individual customer, has been recently renewed on the same terms as in the previous year, including adjustment of price to take care of any increase in the cost

of manufactnre, and if production can be maintained at anything like the level of our capacity, the profits for the year should be satisfactory. I am not taking into account, of coarse, the heavy inroads which may be made on them by the Excess Profits and other taxes.

2. **The Cambodia Mills, Ltd.** Annnal Meeting held in May 1945.

In the first place, you will wish to know how we are buildiog up our position for the future to ensnre, as I hope, the continned prosperity of this Mill as one of the units in the most important industry in this Presidency. The importaot item in this connection is that of the E. P. T. compulsory deposits which we have now to make every year to Government but subject to refund later on. These deposits made and to be made in respect of the year 1943 aod 1944 total Rs. 11,22,000 and in dne course we should receive from Government an additional 50 per cent., thus making a total up to the end of 1944 of Rs. 16,83 000 plus 2 per cent. interest on our own payment. Assuming, as I think it reasonable to assume, that we shall continue to be called on for this E. P T. compulsory deposit for another year or two, it seems probable that we may eventually receive back something in the neighbourhood of Rs. 20,00,000. It is likely that this will only be paid gradully, but, as it will probably take ns even longer to obtain equipment in connection with our proposed post-war expansion scheme, that need not worry us unduly. The main poiot is that, according to our estimates, what we are entitled to receive back by way of our own payment together with Government contribution should prove ample to meet all outlay on the expansion scheme that we visualise, together with a reasonable margin to meet other contingencies.

3. **The Ahmedabad Electricity Co., Ltd.** Annual Meetiog held in February 1941.

"The trade of Ahmedabad has been stimulated by the war and I am confident that the demand for electric power for industrial purpose would be greater than it is already if suitable electric motors were more readily obtainable by prospective consumers.

"The generating costs of yonr station and the cost of maintaining your plant have not so far been affected by the war to any great extent, although as I hinted might be the case io my speech oo this occasioo last year, your Board decided to provide 'staodard of living allowance' to help employees drawing Rs. 50 p. m. or less to meet the increased cost of liviog.

"While on the subject of E. P. T., I would mention that your Board have under consideration the qnestion of certaio tariff revisions and I have reason to believe that as a result of the enhanced capital commitments already incurred and accruing, combined with the effects of the prospective rate reductions, the liability of the Company to E. P. T. on the results of the current year is unlikely to be of great extent, if indeed there will be any at all."

**Yield.** In connection with an estimate of the prospects of a company, it is also useful to calculate the yield on its shares. The term 'yield' means the percentage of income expected on the capital invested in the shares of a company. The yield on the equity shares of a

company is calculated on the basis of their current market prices and the expected annual dividend. The current market quotation to be employed for the purpose of calculating yield should not include any dividend recently declared on the shares, and the expected yearly income will usually be based on the last year's actual dividend increased or decreased, if necessary by the company's future prospects. The exact method of yield computation will now be explained by means of a few examples.

1. A company paid for 1945 a dividend of Rs. 10 per share free of tax on its Rs. 100 fully-paid shares quoted at Rs. 165 ex-dividend. The yield on these shares works out to 6.06% free of tax. That is to say, an investor who purchases one share will have to pay Rs 165 on which he may expect a dividend of Rs 10 if the last year's rate of dividend is maintained. But if the future prospects of the company suggest that the dividend for the current year may be raised to Rs. 12 per share free of tax, then the yield will be 7.3% tax-free.

2. A company paid for 1945 a dividend of 20% free of tax on its Rs. 10 fully-paid shares quoted at Rs 60 cum-dividend. Deducting the accrued dividend of Rs 2 from the cum-dividend quotation, the ex-dividend price comes to Rs. 58 per share, and the yield thereon is 3.45% free of tax.

3. A company paid for 1945 an interim dividend of 8% and a final dividend of 28% on its Rs. 50 fully-paid shares quoted at Rs. 312½ cum dividend. Here the dividend included in the quotation is only the final dividend, namely, Rs. 14 per share. The ex-dividend price works out to Rs 298—8—0 and the expected annual dividend on the basis of the last year's dividend i.e. Rs. 18 per share. Therefore the yield comes to nearly 6%.

4. A company paid for 1945 an interim dividend of 22½% and a final dividend of 22½% on its Rs. 25 fully-paid shares quoted at Rs. 214 ex-dividend. The yield on these shares is 5.26%.

Sometimes the market quotation of the shares of a company includes not only the dividend declared thereon but also the value of rights attached to them. Such a market quotation is known as the cum-dividend cum rights price. The rights referred to in the market quotation may be either a right to the new issues of shares at concessional rates or a right to the free issue of bonus shares. In calculating the yield on a share which is quoted cum-dividend cum-rights, the value of the dividend and the value of the rights included in the quotation must be ascertained and the ex-dividend ex-rights price of the share worked out. How this should be done is described in the following illustration.

A company has an issued and fully-paid share capital Rs. 10,00,000 in Rs. 100 shares. It increases its share capital by the creation of 5,000 new shares of Rs. 100 each, which are to be offered to the existing shareholders at Rs. 205 each in the proportion of one new share for every two old shares held. The company has also declared a dividend of Rs. 15 per share for the last year. The market quotation of the shares after the declaration of dividend and the announcement of

rights is Rs. 265 per share cum-dividend cum-rights. The yield in this case will be computed as follows:—

| | | Rs. |
|---|---|---|
| Cum-dividend cum-rights price | ... | 265 |
| *Less* the amount of dividend included there in | | 15 |
| Therefore the ex-dividend cum-rights price is | | 250 |
| The ex-dividend cum-rights price of two shares which must be bought in order to be entitled to a new share at concessional rate will be | ... | 500 |
| Add the amount to be paid to the company for a new share ... | ... | 205 |
| Therefore the ex-dividend ex rights price of three shares becomes ... | ... | 705 |
| Or, the x d.x.r. price of a share is | ... | 235 |

In other words, the value of rights attached to each share is Rs. 15.

Now a dividend of Rs 15 is expected on a capital of Rs. 235. Therefore the yield comes to 6.4%.

If in the above illustration the company does not issue fresh capital at concessional rates, but it issues one free bonus share for every four shares held, then the yield will be worked out as under.—

The ex-dividend cum rights-price of four shares which must be purchased in order to secure a free bonus share is Rs. 1 000. That is to say, by investing Rs. 1,000 a shareholder becomes entitled to a free bonus share In other words, the ex-dividend ex-rights price of five shares is Rs. 1,000 or the ex-dividend ex-rights price of a share is Rs 200 on which a dividend of Rs. 15 may be expected. Therefore the yield works out to 7·5%.

Take another illustration A company's issued capital consists of Rs 10 fully-paid ordinary shares. It prepares half-yearly accounts and it has just declared a dividend of Rs. 4 per share free of tax for the last half year. It also declares a capital bonus by issuing one free Rs. 10 fully-paid preference share as a bonus share for every five ordinary shares held. After the declaration of the dividend and the capital bonus, the market price of its ordinary shares is quoted at Rs. 92½ cum-dividend cum-rights; and it is also expected that the preference shares issued as bonus shares will have a market quotation of Rs, 15 each. In such circumstances the yield will be calculated as follows :—

| | | Rs. | a. | p. |
|---|---|---|---|---|
| The cum dividend cum-rights price of an ordinaary share ... | ... | 92 | 8 | 0 |
| *Less* the amount of dividend included therein | ... | 4 | 0 | 0 |
| Therefore the x d.c-r. price of an ordinary share is | | 88 | 8 | 0 |

Now for every five ordinary shares held one free preference share is received as a bonus share, and the expected market price of this bonus share is to be Rs. 15. Therefore Rs. 3 is the value of the bonus right attached to each ordinary share; and the ex-dividend ex-rights price of an ordinary share will be (Rs. 88—8—0 minus Rs. 3) or Rs. 85—8—0, on which a half yearly dividend or Rs. 4 or an annual dividend of Rs. 8 is expected. The yield will then come to 9.4%.

**Break-up Value of Shares.** Sometimes it may be necessary to calculate the break-up value of the shares of a company, particularly when their market price is standing at a figure not warranted by the financial position of the company. The break-up value of a share means the amount obtained by dividing the net assets (i e., total assets minus liabilities) by the number of shares issued. The break-up value of the shares of a company may, therefore, be calculated as follows :—

1. *Find out the amount of net assets by deducting from the total assets the amount of liabilities after allowing for a probable loss or a possible profit on the balance sheet values.*

2. If there are shares of one class only, divide the amount of net assets by the number of shares issued, and the resulting figure will be the amount of the break-up value of each share.

3. If there are both ordinary and preference shares, ascertain the rights attached to preference shares in respect of dividend and repayment of capital. Where the preference shares have priority as to repayment of capital on a winding-up, they will be valued at par, and the balance of the net assets will be divided by the number of ordinary shares issued which will give the break-up value of each ordinary share. Where, however, the preference shares have no priority as to the return of capital on a winding up, they rank *pari passu* with the ordinary shares; and the net assets of the company are deemed to be the combined property of the holders of both classes of shares, and will be apportioned between them according to the amount of their paid-up capital. The preference shareholders' portion of the net assets will then be divided by the number of preference shares issued and the ordinary shareholders' portion by the number of ordinary shares issued, thus giving the break-up value of each preference as well as ordinary share.

This principle my be illustrated by means of an example. Suppose the following is the balance sheet of a company as on 31st December 1945 :

| | Rs. | | Rs. |
|---|---|---|---|
| 2,000 6% Preference Shares of Rs. 100 each fully paid | 2,00,000 | Total Assets | 14,00,000 |
| 40,000 Ordinary Shares of Rs. 10 each fully-paid | 4,00,000 | | |
| Reserves | 4 00,000 | | |
| Liabilities | 3,00,000 | | |
| Profit and Loss Account | 1,00·000 | | |
| Total | 14,00,000 | Total | 14,00,000 |

The net assets of this company amount to Rs. 11,00,000. If the preference shares have a priority as to repayment of capital in the event of the company's winding-up, then each preference share is worth Rs. 100, leaving Rs 9 00,000 of the net assets for the ordinary shares. Each ordinary share will then have a break-up value of Rs 22½. If, however, the preference shares rank *pari passu* with the ordinary shares, the net assets of the company amounting to Rs. 11,00 000 will be apportioned between the preference and ordinary shareholders in the ratio of their respective capitals, namely, in the ratio of 1 and 2. The preference shareholders' portion of the net assets will be

Rs. 3,66,666-10-8 and the ordinary shareholders' portion Rs. 7,33,333-5-4. Rs. 3,66,666-10-8 divided by 2,000 will give the break-up value of each preference share; and Rs 7,33,333-5-4 divided by 40,000 will give the break-up value of each ordinary share.

In making these calculations, any contingent assets not appearing on the balance sheet should also be taken into account. At the present time such contingent assets consist of the post-war refunds of E. P. T. paid and the interest payable by Government on the E P.T. compulsory deposit. No company has taken credit in its accounts for the post-war refunds of E.P T. paid; and hardly one or two companies take credit in their accounts for the interest payable by Government on the E. P. T. deposits.

When the published accounts of a company have been examined on the lines suggested above, it will be possible to form a satisfactory opinion regarding its working financial position and prospects. In the case of a good company it may be found that its profits are increasing, that its depreciation and reserve policy is generous, that its dividend performance is excellent, that its capital plan is well-designed, that its reserves are adequate and are represented by liquid resources, that its liabilities are well covered by current assets, that its block is adequately depreciated, that the composition of its current assets is very satisfactory, that its ways and means position is healthy, that its management is in the hands of capable agents and that its future prospects are promising.

The principles of criticism explained in the foregoing pages of this chapter are now to be illustrated by actual reviews of the published accounts of companies which are taken from the columns of the *"Commerce"*.

**1. The Muir Mills Co., Ltd.**

A fall of 21 per cent in the value of turnover, an increase of a little over 11 per cent. in manufacturing expenses a sharp decline of about 41 per cent. in the gross profit, a marked cut of 43 per cent. in the return to ordinary shareholders, complete absence of provision for depreciation, and a reduction of 11 per cent in the transfer to reserves—these are the outstanding features of the financial results of the Muir Mills Co. Ltd. (Managing Directors: Messrs, K. J. D. Price and T. K. Smith—the latter being in military service now) for the year ended 31st December, 1944

Such an all round recession in the results of the Company as noted above is only as it should be, in view of the progressive reduction in the prices of cotton manufactures, coupled with the increase in the incidence of taxation. It may be of interest to note, in this connection, that the percentage of fall in the value of turnover is practically the same as the total cut in the ex-mill prices of cotton manufactures effected by the Textile Control Board in 1944.

Now to mention the actual figures. The turnover of the Muir Mills for the year, as compared with that for 1943, declined in value from Rs. 307.62 lakhs to Rs 254.03 lakhs, while the total expenditure recorded a fairly substantial rise from Rs. 155.08 lakhs to Rs. 164.81 lakhs. In the result, the gross profit has been markedly lower at Rs 90.19 lakhs, as against Rs. 152.98 lakhs for 1943 In other words, the fall in the gross profit is as much as Rs. 62.79 lakhs. Consequent

upon this sharp decline, the year's allocations have naturally experienced an all-round fall. The provision for taxation has been reduced from Rs. 115 lakhs to Rs 67 lakhs—a cut of Rs 48 lakhs. This reduction is an approximate indication of the extent to which the Government's revenue has been adversely affected, thanks to the introduction of the price control in the interests of consumers The return to ordinary shareholders, too, has been curtailed from 70 per cent to 40 per cent. by reducing the rate of bonus from 50 per cent to 20 per cent. Perhaps a much larger cut would have been necessitated had the Directors decided on providing for depreciation on the previous year's scale of Rs. 7 lakhs, instead of setting apart nothing at all as they have done now. The transfer to reserves also has been reduced from Rs. 18 lakhs in the preceding year to Rs. 16 lakhs in the year under review. This sum is equivalent to the estimated sum payable to the Government in 1945 by way of E.P.T. compulsory deposit. Inasmuch as the transfer to reserves has been made, both last year as well as this year, with the primary object of earmarking sums sufficient to pay the E P. T. compulsory deposit, the reduction in this year's provision for reserve is understandable.

The following comparative table showing the results of the Company for the past four years, as also those for the semi-pre-war year of 1939, clearly brings out the outstanding features of the results for the year under review :—

( In lakhs of rupees )

| | Year ended 31st December | | | | |
|---|---|---|---|---|---|
| | 1944 | 1943 | 1942 | 1941 | 1939 (Pre-war) |
| Turnover (sales) ... | 254.03 | 307.62 | 183.68 | 117.37 | 66 51 |
| Manufacturing expenses ... | 111.18 | 99.62 | 69.63 | 57.00 | 37 23 |
| Establishment charges ... | 53 63 | 55 46 | 38.21 | 24.69 | 20 14 |
| Gross profit ... | 90.19 | 152.98 | 76.23 | 35.82 | 9.15 |
| Provision for— | | | | | |
| Taxation ... | 67 00 | 115.0[illegible] | 56.00 | 25 50 | 2 75 |
| Depreciation ... | Nil | 7.00 | 9.00 | 4.50 | 2.00 |
| Net profit ... | 23.15 | 30.93 | 11.18 | 5.77 | 4.33 |
| Dividends— | | | | | |
| Preference ... | 6% | 6% | 6% | 6% | 6% |
| Ordinary ... | 20% | 20% | 20% | 20% | 20% |
| Bonus to (a) ... | 20% | 50% | 30% | 10% | 3% |
| Total amount distributed to (a) ... | 6.00 | 10.50 | 7.50 | 4.50 | 3.45 |
| Transfer to Reserve ... | 16 00* | 18 00† | Nil | Nil. | Nil. |
| Carry forward ... | 4.48 | 4.84 | 3.91 | 1.72 | 1.26 |

(a)=Ordinary shareholders * General reserve fund.

† Deferred mill renovation reserve.

The most notable feature as revealed by the table published above is that the total distribution to ordinary shareholders is lower than that for 1942, even though such is better than that for 1941

Neither the reduction in the transfer to the reserve fund nor the absence of any provision for depreciation affects the financial position

of the Company to any material extent, for, in the past, the management has conserved the resources of the Company in a very judicious manner, as the following summarised version of its latest balance-sheet will testify :—

| Liabilities | | Rs. | Assets | | Rs. |
|---|---|---|---|---|---|
| | | | Gross Block | ... | 107,06,578 |
| Capital* | ... | 30,00,000 | *Less*— | | |
| | | | Depreciation | ... | 83,33,516 |
| Reserves and surpluses | | 78,48,312 | | | |
| | | | Net Block | ... | 23,73,062 |
| Liabilities † | ... | 89,80,166 | Stores | ... | 15,96,464 |
| | | | Stocks | ... | 57,33,076 |
| | | | Debts, Deposits and Advances | ... | 45,78,702 |
| | | | Investments | ... | 29,11,142 |
| | | | Cash | ... | 26,36,032 |
| | Rs. | 1,98,28,478 | | Rs. | 1,98,28,478 |

*Half of this capital consists of perference shares carrying interest at the rate of 6 per cent., tax free. These shares were issued as bonus shares.

† Include provision for taxation as also the final dividends and bonus to shareholders.

It will be noted from the foregoing that the reserves are more than 2½ times the paid-up capital. All liabilities are well covered by floating assets, of which a large proportion is of high liquidity. For instance, of the total investments, as much as Rs. 25.67 lakhs represent investments in Government securities. The market value of all investments is greatly in excess of that shown above. Again, the total of Rs 45.78 lakhs shown against "debts, deposits and advances" includes Rs. 30.38 lakhs, being deposits with the Government of India under section 10 of the Finance Act of 1940.

At the time of writing, the Rs. 50 paid up ordinary shares of the Company are quoting at Rs 427-8, *cum* final dividend and bonus, namely, Rs 15, as against Rs. 510 a year ago and Rs. 400 two years before. On the basis of the latest quotation and that of total distribution for 1944, the yield on these shares works out to about 4.8 per cent free of tax.

As regards the prospects for the current year, while we do not desire to make any prophecy, we may point out that generally speaking, ex mill ceiling prices of cotton manufactures at present are some 28 per cent less than those that were obtaining in the first quarter of 1944, whereas the cost of production is practically the same or only a shade lower than that in the preceding year. In other words, the margin of profit has appreciably been reduced This, together with the fact that the present incidence, and the system, of taxation leaves only a very small proportion of the profit for distribution to shareholders, leads to the irresistible conclusion that the cotton mill dividends for 1945 cannot but be lower than even that for 1944. In the case of first class companies like the Muir Mills which have large reserves, however, it may be

possible to maintain the dividend at the 1944 level by reducing the transfers to reserves and depreciation. But the continued adoption of such a policy would not be feasible, besides being obviously unsound and short sighted. (The "*Commerce*" dated 10-2-1945)

**2. The Bengal Coal Co, Ltd.**

An increase of nearly cent per cent in the gross profit is the outstanding feature of the financial results of the Bengal Coal Co., Ltd. (Managing Agents: Messrs. Andrew Yule & Co., Ltd. Calcutta) for the half-year ended 31st October, 1944, as compared with those for the previous half year. Other notable features of the result are an increase in the provision for taxation and cesses of Rs 20 34 lakhs to Rs. 38 lakhs, the transfer, for the first time after many years, of a sizable amount of Rs 3 25,000 to reserves, and the raising of the rate of distribution to shareholders by one-third, that is, from 24 per cent per annum to 32 per cent. per annum. As compared with those for the corresponding half-year of 1943, the results for the half year under review disclose even more impressive improvements, as will be evident from the following comparative table :—

(Value in rupees)

| | Half year ended | | |
|---|---|---|---|
| | 31-10-1944 | 30-4-1944 | 31-10-1943 |
| | Rs. | Rs. | Rs |
| Sales of coal ... | 1,64,80,717 | 98,95,236 | 78,05,333 |
| Othe Income ... | 4,51,087 | 3,78,366 | 3,56,249 |
| Stock ... | 7,87,771 | 5,32,586 | 1,63,614 |
| Coal purchases ... | 64,17,285 | 26,75,340 | 15 23,497 |
| Working expenses ... | 52,53,826 | 51,34,397 | 44,33,903 |
| Gross profit ... | 55,15,879 | 28,32,836 | 18,13,245 |
| Transfer to— | | | |
| Taxation and cess reserve ... | 38,00,000 | 17,66,374 | 9,25,000 |
| Depreciation ... | 3,00 000 | 3,00,000 | 3 00 000 |
| Reserves ... | 3,25,000 | ... | ... |
| Dividend ... | 4,00,000 | 4,00,000 | 4,00,000 |
| | 20% p. a. | 20% p. a | 20% p. a. |
| Bonus to Shareholders ... | 2,40,000 | 80,000 | 80,000 |
| | 12% p. a | 4% p a | 4% p. a. |
| Carry forward ... | 2,72,478 | 1,83,485 | 96,441 |
| | Tons | Tons | Tons |
| Raisings ... | 723,283 | 762,537 | 784,398 |
| Despatches ... | 1,190,749 | 913,398 | 988,661 |

p. a,=per cent per annum

As will be seen from the foregoing table, raisings for the half-year under review have been the lowest, which, according to the Directors, is due to continued scarcity of mining labour. If, in spite of this. the profit discloses a remarkable improvement, it must be attributed partly to the increase in the selling price of coal and partly to the rise in the quantity of coal purchased and sold to consumers. The extent of the

improvement in the latter can be ganged to a certain extent, from the figures relating to despatches inclnded in the comparative table above. Thanks to higber prices and larger despatches. sale proceeds for the half year under review stand at the impressive level of Rs. 164.80 lakhs—which we presume must be a record in the bistory of this century-old company. It is not nnlikely that the gross profit at Rs. 55.15 lakhs also is a new high record.

As compared with the corresponding half-year of the preceding year, while sale proceeds are higher by a little over 100 per cent. the gross profit, it is noteworthy, shows a rise of well over 200 per cent. But what is the proportion of this large increase that goes to the Company? A glance at the table will show that such is very small, for, out of the gross profit of Rs 55.15 lakhs, Rs. 38 lakhs, or about 70 per cent., represent provision for taxation and cesses. As compared with the half year ended 31st October, 1943, this provision discloses an increase of 300 per cent. All these unmistakably suggest that the coal industry has now stepped into the shoes of the cotton mill industry, which, until recently, has been enjoying the distinction of being "the unofficial and unpaid agency for the easy collection of the Government's direct taxation."

The transfer of Rs. 3,25,000 to reserves is, it must be mentioned here, made up of Rs. 1,00,000 to reserve for amenities for miners and their families, and of Rs 2,25,000 to reserve against reduction in valuation of stores Both the provisions reflect the far-sightedness of those who are at the helm of the Company's affairs. It is needless to add that. in the future order of things, more than ever before, a contented labour will be the first essential requisite for the continued success of the Company, and this cannot be achieved unless proper amenities are provided for the workers The provision of a lakh of of rupees shows that the Directors are alive to this point. The earmarking of a substantial sum of Rs 2,25,000 as reserve against reduction in valuation of stores is doubtless born out of the correct comprehension that, once the present emergency ceases, the prices of stores will appreciably decline.

**Excellent Finances**

The finances of the Company are excellent. Its latest balance-sheet is a perfect picture of strength and one which befits its age and the prominent position it commands in the Indian coal industry. The following table, containing the synopsis of the balance sheet of the Company as at 31st October, 1944, and 31st October, 1943, will fully bear out this statement :—

| | As at 31-10-1944 | As at 31-10-1943 | Change over 31-10-1943 |
|---|---|---|---|
| **Liabilities** | Rs. | Rs. | Rs. |
| Capital ... | 40,00,000 | 40,00,000 | ... |
| General reserve fund . | 55,00,000 | 55,00,000 | ... |
| Other reserves and surpluses* | 12,49,428 | 7,48,391 | +5,01,037 |
| Reserve for taxation and cesses ... | 1,02,10,011 | 49,54,011 | +52,56,000 |
| Liabilities† ... | 77,40,821 | 29,87,034 | +47,53,787 |

*Include the amount left undisturbed.

†Including such in respect of the dividend for the respective years.

| Assets | | | |
|---|---|---|---|
| Gross block | 2,70,63,314 | 2,68,03,298 | +2,60,016 |
| Less—Depreciation | 1,90,40,569 | 1,84,61,009 | ... |
| Net block | 80,22,745 | 83,42,289 | — 3,19,544 |
| Stocks and Stores | 40,43,983 | 31,73,068 | +8,70,915 |
| Debts, deposits and advances | 1,17,91,488 | 49,92 155 | +67,99,333 |
| Investments | 8,57,366 | 8,57,175 | + 191 |
| Cash | 39,84,678 | 8,24,749 | +31,59,929 |
| Total | 2,87,00,260 | 1,81,89,436 | +1,05,10,824 |

The increase of well over rupees one crore in the balance sheet total, as will be seen from the foregoing table, generally reflects the highly satisfactory results obtained in the past one year and the marked expansion in the value of turn over brought about chiefly by the inflationary conditions that obtained in the country.

A noteworthy feature as disclosed by the same table is the predominance of floating assets which amount to Rs. 207 lakhs out of the total assets of Rs. 247 lakhs. It will be observed that, over the year as a whole, the liquidity of the Company's assets has recorded a remarkable improvement This will be even more apparent if it is borne in mind that, of the Rs. 117.91 lakhs representing debts, deposits and advances, about Rs. 42.48 lakhs consist of debts due from the Government.

From the Directors' Report to the shareholders it appears that the Company still suffers from scarcity of labour. The Directors, however, hope that "the mining machinery for which the Company is waiting will arrive and be put into use during the coming year and that this will have a beneficial effect on production." In the meanwhile available indications point to the maintenance of, if not a perceptible increase in, the results disclosed above during the current year. The Rs. 100 paid-up ordinary shares of the Company, which were standing in the neighbourhood of Rs. 700 before the announcement of the results shot up to Rs. 730, and are now being quoted at about Rs. 723 which compares with Rs. 590 a year ago and Rs. 395 two years before. Although the level at which these shares now stand might appear to be very high, it cannot be said to be unduly high as, even at this level, the yield works out to 4.5 per cent. free of tax. which considering the encouraging prospects and the excellent finances of the Company, can be regarded as satisfactory. The "*Commerce*" dated 20-1-1945.

3. The Belapur Co., Ltd.

As anticipated in our issue of 24th November last, the profit of the Belapur Co., Ltd., for the year ended 30th September, 1945 (Managers: Messrs. W. H. Brady & Co., Ltd., Bombay) has recorded a noticeable recession, as compared with the previous year. The net profit for the year under review, after providing a sum of Rs. 2,36,932 for depreciation, amounts to Rs. 9,94.198 which compares with Rs. 12,55,469 for the preceding period. The decline in profit which works out to nearly 21 per cent., is mainly due to the sharp rise in the cost of cane cultivation etc, which has gone up from Rs. 14.22 lakhs to Rs. 19.29 lakhs. The increase in the cost of cultivation is mainly due to the acute shortage of

labour for cultivation and harvesting and the consequent higher wages, as also the rise in price of other materials. At the same time, supplies of fertilisers were somewhat irregular.

Sales of sugar at Rs. 52.21 lakhs for 1944—45 are the highest for the past six years. The improvement in the sales receipts must be attributed to the slight increase in the price of sugar sanctioned by the Government and also to the large carry-over of stocks of sugar brought in from the previous year. Despite improved sales, there has not been a corresponding rise in profits owing to increased cost of production for reasons already outlined On the contrary, there has been a slight decline, but, in spite of it, the transfer to depreciation has been maintained at more or less the same level as in 1943—44; to be precise, it is Rs. 2,37 lakhs in 1944—45 as against Rs. 2,53 lakhs in 1943—44. Provision for taxation too is kept unchanged at Rs. 3 lakhs, while a sum of Rs. 25,000 has been earmarked as reserve for crop insurance fund. A further sum of Rs. 50,000 has been set apart as provision towards the Company's scheme for housing labourers as against Rs. 1 lakh in the preceeding year. Presumably, on account of the fall in the profit during the year under review, the management could not allocate anything towards general reserves, whereas, during last year, it was able to provide a sum of Rs. 1.25 lakhs for this purpose, besides setting apart Rs. 25,000 for contingencies fund. The return to shareholders also has been affected these being remunerated at 16 per cent. per annum on their holdings, as against 18 per cent. in the preceding year.

The following table gives, in a nutshell, the progress of the Company during the last six years :—

(In thousands of rupees)

| | Year ended 30th September | | | | | |
|---|---|---|---|---|---|---|
| | 1945 | 1944 | 1943 | 1942 | 1941 | 1940 |
| | Rs | Rs. | Rs. | Rs. | Rs | Rs. |
| Sale of sugar ... | 52,21 | 44,30 | 41,53 | 30,66 | 29,67 | 38,06 |
| Excise duty paid ... | 7,10 | 6,75 | 6,66 | 5,71 | 7,00 | 5,94 |
| Depreciation ... | 2,37 | 2,53 | 2,42 | 1,96 | 42 | 1,06 |
| Profit ... | 9,94 | 12,55 | 12,67 | 7,19 | 6,70 | 14,01 |
| Transfer to— | | | | | | |
| Reserve fund ... | .. | 1,25 | 1,25 | 1,00 | .. | 1,00 |
| Other funds ... | 75 | 1,50 | 1,75 | 1,15 | 15 | 1,19 |
| Taxation reserve ... | 3,00 | 3,00 | 2.50 | 75 | 2,60 | 4,25 |
| Dividend ... | 16% (6,01) | 18% (6,76) | 18% (6,76) | 12% (4,51) | 14% (5,25) | 14% (5,26) |
| Bonus ... | ... | ... | .. | .. | .. | 6% |
| Carry forward ... | 10 | 12 | 27 | 5 | 27 | 34 |

The financial position of the Company is quite sound. During the last four years, the net block value of the Company has been steadily brought down from 36.14 lakhs to Rs. 28.92 lakhs, while reserves and other funds have gradually improved from Rs. 11.98 lakes to Rs. 18.28 lakhs Its liabilities are more than covered by liquid assets, and it is noteworthy that, within the last two years, the management has impressively increased its investments from a mere Rs. 12,546 to Rs. 12.10

lakhs. In this connection, the following comparative table, showing the Company's financial position, as at the close of each of the past four years, will be read with interest.

| | As at 30th September | | | |
|---|---|---|---|---|
| | 1945 | 1944 | 1943 | 1942 |
| | Rs. | Rs. | Rs. | Rs. |
| **Liabilities** | | | | |
| Capital ... | 37,59,800 | 37,59,800 | 37 59,800 | 37,59,800 |
| Reserve, other funds and surpluses* ... | 18,28,131 | 17,54,501 | 15,19,795 | 11,98,160 |
| Reserve for taxes ... | 10,39,225 | 10,25,280 | 7,35,209 | 6,88,460 |
| Liabilities† ... | 10,55,746 | 12,31,732 | 10,76,331 | 9 38,492 |
| **Assets** | | | | |
| Block ... | 28,92,038 | 31,08,346 | 33,75,563 | 36,14,392 |
| Stores, etc. ... | 8,50,839 | 7,41,007 | 5,74,409 | 6,22,050 |
| Stocks ... | 5,14,777 | 8,24,684 | 4,40,757 | 2,60,421 |
| Crop-in progress ... | 15,48,269 | 17,33,095 | 17,72,124 | 12,34,534 |
| Book debts and advances ... | 2,46 613 | 1,85,890 | 1,22,140 | 70,568 |
| Investments ... | 12,10,808 | 8,11,153 | 12,546 | 2,05,885 |
| Cash ... | 4,19,558 | 3,67,138 | 7,93,596 | 5,77,062 |
| Total ... | 76,82,902 | 77,71,313 | 70,91,135 | 65,84,912 |

* Include the carry forward.

† Include the liabilities in respect of the dividends proposed for the respective years.

The immediate outlook for the Company, however, is not altogether encouraging, for, as the Directors themselves suggest in their report, the diversion of sugarcane land to foodcrops, as a result of orders issued by the Government of Bombay, has materially affected the area of cane available for the 1945—46 season. Again, it has been necessary to turn over part of the Company's agricultural labour force to the cultivation of food crops, which would appear to have further aggravated the difficult labour position. Moreover the growing crops to be harvested in 1945—46, we are told, are not as satisfactory as would appear to be usual with the Company, on account of a partial failure of the rains. But the inherent soundness of the concern should not be judged by these transient factors

The "*Commerce*" dated 8—12—1945

**4. The Titaghur Paper Mills Co., Ltd.**

The results of the Titaghur Paper Mills Co., Ltd., for the half-year ended 30th September 1945, reveal no marked variation over those for the previous half-year, but show appreciable improvement as compared with the corresponding half-year of the previous year. The said improvement is, of course, confined only to sales, and gross and net profits while the return to shareholders has been kept unchanged at As. 12 per share (of Rs. 5 each) or 30 per cent. per annum. Even the mode of this distribution has not been changed it being made up of a dividend of As. 8 per share and a bonus of As. 4 per share. Although there has thus been no rise in the distribution to shareholders, the transfer to the reserves has been substantially stepped up.

Just before the results of the Company for the half-year under review were made known to the public, there was a sudden spurt in the value of its ordinary shares from about Rs. 37-8 to Rs. 43-8. The fact that there has been no increase in the return to shareholders, however, has not had any adverse effect on the value of the shares which are still having good enquiries even at as high a price as Rs. 46. A year ago, they were being quoted at only Rs. 29-12. Why is it so? The answer is obvious, namely, the sound financial position of the Company, the probabilities of capital extensions in the post-war years and the chances of the shareholders participating once again in the resources.

To revert to the working of the Company during the half-year under review. The Directors' remarks suggest that the half-year must have been quite satisfactory, a fact which is also borne out by the actual result They observe :

"During the half-year, the mills have been operating at full production, and due to a slight improvement in railway transport facilities, the difficulties experienced in previous half-years regarding the supply of essential raw materials has slightly lessened, although the position cannot be regarded by any means as secure

"Manufacturing costs may be considered satisfactory in view of the continued high prices of all essential raw materials. These costs, however, are still greatly in excess of pre-war standards.

"Government prices during the half-year show a slight reduction. Government offtake for the first three months was reduced, but it was later increased to the percentage taken in the previous half-year."

As for a detailed account of the results of working readers' attention is invited to the following comparative table which is self-explanatory :

(In lakhs of rupees)

| | Six months ended | | | |
|---|---|---|---|---|
| | 30-9-45 | 31-3-45 | 30-9-44 | 31-3-44 |
| Paper sales ... | 169.14 | 177.14 | 142.38 | 133.24 |
| Stock of paper ... | 6.01 | 7.36 | 9.98 | 5.36 |
| Expenses ... | 105.46 | 110.74 | 101.53 | 90.52 |
| Gross profit ... | 62.55 | 63.89 | 45.66 | 39.42 |
| Agents' commission | 2.91 | 3.09 | 2.57 | 2.56 |
| Provision for— | | | | |
| Taxation ... | 41.07 | 42.93 | 32.77 | 24.56 |
| Depreciation ... | 3.23 | 3.68 | 3.91 | 3.99 |
| Net profit ... | 14.95 | 13.75 | 12.68 | 11.92 |
| To reserves ... | 7.62 | 6.18 | 5.00 | 4.50 |
| To other funds ... | 1.10 | 1.10 | 1.00 | 1.00 |
| Dividends— | | | | |
| Fixed ... | 1.05 | 1.05 | 1.05 | 1.05 |
| Ordinary .. ... | 5.25 (15%) | 5.25 (15%) | 5.25 (15%) | 5.25 (15%) |
| Carry forward ... | 3.21 | 3.28 | 3.02 | 2.64 |

*N. B.*—Ordinary dividend includes a bonus of As. 4, or 5 per cent. for the half-year, per share.

The company has paid; according to the Directors, a sum of Rs. 47.59 lakhs by way of compulsory and voluntary E. P. T. deposits. A further sum is still due to be paid in respect of 1944-45 excess profits. Against this obligation and previous deposits made, a further sum of Rs 5 lakhs has been set aside this half-year for deferred mill renovations, thus earmarking this amount for future capital replacements. The total amount standing to the credit of this account is now as much as Rs. 32.52 lakhs.

The financial position of the Company is excellent, being in keeping with the leading position it occupies among the paper manufacturers in India and with its age and also the tradition of the management. The capital of the Company is Rs 65.89 lakhs, of which Rs. 31.83 lakhs represent reserves capitalised in the past, once in 1937 (Rs. 14.32 lakhs) and, again, in 1941 (Rs 17.51 lakhs). Besides this capital, the Company has debentures to the tune of Rs. 25 lakhs, as against which it has a debenture-redemption reserve of Rs. 25 lakhs which is separately invested in Government securities as also in its own debentures (Rs. 3. 45 lakhs). Apart from this reserve, the Company has other reserve funds and surpluses aggregating to Rs. 60.59 lakhs, against which there are investments in Government securities amounting to Rs 60.72 lakhs. These reserves exclude Rs. 7.65 lakhs, being the provision for the labour quarters and labour welfare Reserve for taxation amounts to Rs. 54.37 lakhs Liabilities aggregate Rs 77.95 lakhs, including such in respect of dividend for the half-year under review.

On the assets side, the net block is shown at Rs. 58.41 lakhs. It may be noted that the gross block is as much as Rs. 267.36 lakhs; in other words, the total depreciation that has so far been provided is no less than Rs. 208.95 lakhs. Stocks are shown at Rs. 63.70 lakhs, book debts and advance at Rs. 58.91 lakhs, deposits with the Government at Rs. 47. 59 lakhs, and cash at Rs. 2. 11 lakhs. In short, the most noteworthy feature of the Company's finances is the preponderance of floating assets, the bulk of which is of a highly liquid type.

The precise financial position of the Company will be even more clear and better appreciated from the following synopsis of the Company's balance-sheet as at 30th September, 1945 .—

| Liabilities | Rs. | Assets | Rs. |
|---|---|---|---|
| Capital ... | 65,89,000 | Block (net) ... | 58,40,950 |
| Debentures ... | 25,00,000 | Stocks ... | 63,70,206 |
| Liabilities ... | 77,95,570 | Book debts and advances | 58,91,222 |
| Reserve for taxation ... | 54,37,180 | Deposit with Government ... | 47,59,165 |
| Reserves, other funds and surplus ... | 93,24,804 | Investments ... | 85,73,824 |
| | | Cash ... | 2,11,187 |
| | Rs. 3,16,46,554 | | Rs. 3,16,46,554 |

*N. B.*—In the above account, no credit has been taken for amounts which will be repayable by the Government from E. P. T. on account of optional or compulsory deposits. Similarly no credit has been taken for interest accruing on these deposits.

Two important changes are likely to take place in the finances of the Company during the current year. The first of these is consequent on the fact that the 5 per cent second cumulative perference shares, amounting to Rs. 15,00,000, are redeemable on 30th September, 1946, at a premium of 5 per cent. of the face value (Rs 100 per share). In view of the strong financial position of the Company, the management can, if it so desires, redeem them, or if it is in need of cash for a relatively more profitable purpose, it may issue debentures for a similar amount, but at a relatively lower rate of interest, say, at about 3 or 3½ per cent. The other change which appears to be certain is the redemption of the debentures of the value of Rs. 25 lakhs carrying interest at 4½ per cent. and falling due on 31st March, 1946 The debenture sinking fund has already reached the figure of the outstandings and is separately invested. There will, therefore, be no difficulty in paying off this secured liability and when it is fully discharged, the reserve specifically relating to it should be available for capitalisation and issue of bonus shares. The only point to be considered in this connection is whether the Company will be able to maintain the dividend at the present level of 30 per cent. per annum, or even at a slightly lower level, on the capital so increased. We are of the opinion that it should be possible for the Company to do so, considering that it has been, in the past, able to provide substantial sums for reserves, besides paying interest on these debenturers and a more handsome dividend on ordinary shares.

Further, the prospects for the paper industry in this country are so encouraging that the Company may be able at least to maintain the present level of earnings if not show an improvement thereon. With the spread of literacy that must follow the intensive literacy drive now afoot, consumption of paper in India should easily go up by leaps and bounds in the years to come and the Company would be required to expand its productive capacity if it were to participate in the widening market for paper. Besides the possibilities in this country, the Indian paper manufacturers will find a ready market in the neighbouring countries also. And Titaghur, with its vast experience, up-to-date production equipment, and reputation for production quality goods, should be able to get a substantial share of this export trade

The "*Commerce Dated 26. 1. 46.*

5. The Bank of India, Ltd.

The Central Bank of India Ltd. is the second largest institution among the joint-stock commercial banks in India alike in regard to the resources and the area served Its statement of accounts covering the year ended 31st December, 1943, therefore, fully reflects the general trend of progress of the Indian banking system as a whole. Readers of *Commerce* will have doubtless noted that the main features of banking trends for 1943 are a record expansion in deposits and substantial increases in advances, cash and investments, as also in earnings. The deposits of scheduled banks as a whole, for instance, rose, during 1943, from Rs. 335 06 crores to Rs. 500.82 crores, that is, by no less than Rs. 165 crores. Their advances and bills discounted increased by 69.26 crores to Rs. 167.60 crores and their cash balances by Rs. 40.79 crores to Rs. 105.88 crores Exact figures relating to investments of scheduled banks are not available but, on a rough estimate, it is found that they must have gone up by about Rs. 55 to Rs. 60 crores.

Judged against this general background, the Central Bank's progress during the year is indeed quite impressive. A study of its latest balance sheet, full details of which are published elsewhere in this issue, in conjunction with that as at the close of 1942, shows that deposits have shot up from Rs. 59.65 crores to Rs. 81.64 crores that is, by about Rs. 22 crores. On the assets side, investments are higher by Rs. 10.64 crores and advances by Rs. 10.57 crores to stand at Rs. 44.70 crores and Rs. 26.58 crores respectively. Cash balances have moved up from Rs. 13. 96 crores to Rs. 17 35 crores, the precise increase heing Rs 3.39 crores. The total resources of the Bank, as represented by its balance sheet total, amount to Rs. 92.17 crores, as against Rs. 68.16 crores at the close of 1942.

From the foregoing account it will be observed that the Bank has been able to find fairly remunerative outlets for practically the entire increase in its deposits. Thus, of a rise of Rs, 22 crores in the latter, advances and bills, the best remunerative assets in the portfolio of a commercial bank, have accounted for nearly 50 per cent. and the investments for the remaining 50 per cent. As the investment consists mostly of Government securities and no Treasury Bills and a small percentage of equities, the return on such must have been fairly high. The Cumulative effect of these two factors is reflected in the Bank's earnings (for the year under review) which stand at the astoundingly high level of Rs. 108,35 lakhs, as against a mere Rs. 49.51 lakhs for 1942 and Rs. 43.50 lakhs for 1941 and Rs. 36.56 lakhs for 1940 Thus as compared with the previous year, the increase works out to Rs, 58.84 lakhs, or about 108 per cent. Such a phenomenal rise is indeed a memorable achievement in the history of the Bank. It is no exaggeration when we say that this achievement fully redounds to the credit of the management, for it should be noted that the increased earnings are the result of a well thought out and courageous investment policy and not due to any windfall by way of capital appreciation realised on sale of investments as some used to believe. It may be added here that the profit on sale of investments for the year under review has been no more than Rs. 74,191, which is about a fraction of the gross total income of Rs. 227,28 lakhs.

How this large profit of the Bank for the year under review has distributed by the Board of Directors is by now well known, thanks to the preliminary announcement of the result early this year. The Directors have raised the dividend level from 8[1] percent per annum for 1942 to 10 per cent, besides maintaining the bonus to shareholders at 2 per cent per annum. The total distribution to shareholders, therefore, amounts to 12 per cent per annum, which compared with 10 per cent for 1942 and 9 per cent for 1941 as well as 1940. It may be mentioned here that the proposed distribution of 12 per cent for the year under review is the highest for the past two decades and probably the highest in the history of the Bank.

As in the case of industrial companies, the Bank's earnings have been subject to heavy incidence of taxation This will be evident from the fact that, out of a profit of Rs. 108.35 lakhs, the Directors have earmarked no less than Rs. 60 lakhs for taxation as against only Rs 10 lakhs in the previous year and Rs. 8 lakhs in 1941.

The Directors have very wisely taken the present favourable conditions further to strengthen the reserve of the Bank. Thus they,

have raised the transfer to reserve and contingency account from Rs. 7 lakhs to Rs. 12 lakhs This, it should be noted, is besides maintaining the allocation to investment reserve at Rs. 5 lakhs and Rs. 3.33 lakhs to sinking fund.

What we have stated above is but a brief description of the salient features of the Bank's results for the year under review. For a fuller account we invite the readers' attention to the following comparative table :—

( In Thousands )

| | Year ended 31st December | | | |
|---|---|---|---|---|
| | 1943 | 1942 | 1941 | 1940 |
| **Receipts** | Rs. | Rs. | Rs. | Rs. |
| Interest and discount ... | 1,93,46 | 1,16 88 | 1,10,94 | 1,02,58 |
| Total income ... | 2,27,28 | 1,42,74 | 1,32,10 | 1,21,61 |
| **Expenditure** | | | | |
| Interest on deposits .. | 41,87 | 36,95 | 38,88 | 39,91 |
| Salaries ... | 53,03 | 36,52 | 31,68 | 28,97 |
| Other expenses .. | 24,03 | 19,75 | 18,02 | 16 16 |
| Profit* ... | 1,08,35 | 49,51 | 43,50 | 36,56 |
| To depreciation .. | 90 | 77 | 77 | 76 |
| To sinking fund ... | 3,33 | 3,33 | 3,45 | 3,32 |
| To reserve and contingency fund ... | 12,00 | 7,00 | 7,00 | 7,00 |
| To taxation ... | 60,00 | 10,00 | 8,00 | 3,00 |
| To investment reserve ... | 5,00 | 5,00 | 5,27 | 5,00 |
| To dividend and bonus to shareholders† ... | 20,17 (12%) | 16,81 (10%) | 15,13 (9%) | 15,13 (9%) |
| To bonus to staff ... | 6,60 | 5 50 | 3,00 | 2,30 |
| To carry forward ... | 10,42 | 10,03 | 8,98 | 8,14 |

* Before providing for taxation and depreciation.

† Includes bonus of 2 per cent.

It will be observed from the above table that, of an increase of Rs. 59 lakhs in the profit, provision for taxation absorbs as much as Rs. 50 lakhs, leaving only an extra of Rs 9 lakhs available for allocation. The bulk of this balance is devoted to enrich the reserves, the extra amount required to meet the rise in the dividend level being only Rs. 3,36 lakhs The fact that the carry forward is higher than the sum brought in clearly indicates that all the allocations, including the dividend, have been fully earned and that there has been no occasion to draw from the undistributed profits of the previous years.

We stated earlier that the Bank's investments have gone up by Rs 10 64 crores. Of this over Rs 8.29 crores have been accounted for by Government of India terminable loans about Rs. 2.07 crores by non-terminable loans. There has been a small increase of about half a-crore in industrials also. Total investments (exclusive of accrued interest and those in subsidiaries aggregate Rs. 44.32 crores, their market value being much higher at Rs 46.70 crores. Of the total investments Rs. 44.32 crores, it is noteworthy, Government securities

alone account for Rs 40.58 crores which is equivalent to 43 per cent. of the total assets. This is a clear indication of the extent to which the Bank is directly placing its resources at the disposal of the Government to finance the war.

Now to turn to the balance sheet of the Bank. We have already indicated the outstanding features thereof and therefore need not go into them again at greater length. We, however, give below a comparative table, a perusal of which will enable one easily to appreciate the excellent progress made by the Bank during the year under review :—

(In thousands)

| | As at 31-12-43 | As at 31-12-42 | As at 31-12-41 | As at 31-12-40 |
|---|---|---|---|---|
| | Rs. | Rs. | Rs. | Rs. |
| Capital ... | 1,68,13 | 1,68,13 | 1,68,13 | 1,68,13 |
| Reserve fund ... | 1,20,00 | 1,08,00 | 1,01,00 | 94,00 |
| Sinking fund ... | 48,22 | 40,31 | 35,42 | 30,02 |
| Deposits ... | 81,63,71 | 59,65,34 | 41,31,90 | 32,49,88 |
| Cash ... | 17,35,31 | 13,96,35 | 6,72,32 | 9,02,31 |
| Investments ... | 44,70,48 | 34,06,32 | 21,05,52 | 12,95,11 |
| Advances ... | 25,58,83 | 16,01,15 | 18,84,72 | 13,36,01 |
| Land and buildings ... | 1,03,89 | 1,11,56 | 1,18,85 | 1,18,70 |
| % of cash to deposits ... | 20.7 | 23.3 | 13.8 | 28 |
| % of liquid assets to deposits ... | 55 | 80 | 67.1 | 68.75 |
| % of advances to deposits | 31.9 | 26.3 | 46.3 | 40.6 |

Turning to the full details of the balance-sheet published elsewhere in this issue, one will find that the Bank holds no Treasury Bills of the Government of India but only those of the British Government amounting in all to Rs. 66.66 lakhs. A year ago, it may be noted, the Bank had no British Government Treasury Bills but only the Government of India Bills aggregating as much as Rs. 185 lakhs. This switch over is doubtless an extraordinary feature and as such deserves more than a passing reference. What has made the Bank to prefer sterling Treasury Bills instead of rupee Treasury Bills? We believe that it must have been due purely to considerations of yield. The British Treasury Bills have been as readers may be aware, giving a steady yield of 1 per cent while the return on those of the Government of India has been only about ¾ per cent except in the first half of 1943. Further, the yield on Indian Bills declined to as low as 11/16 per cent. towards the close of 1943 with the result that the British Bills were relatively attractive at that time. Incidentally, this switch over from the Government of India Bills is a distinct pointer to the Bank's faith in sterling.

As was anticipated in these columns, sometime ago, the Directors have decided to increase the capital. Full details of the proposal have been published in our last week's issue. According to these the authorised capital is to be increased from Rs. 3,50 crores to Rs. 5.25 crores by the creation of 3,5 lakhs shares of Rs 50 each, of which Rs. 25 will be paid-up. This will raise the paid-up capital to Rs. 262.50 lakhs. Of the total of 3,77,472 new shares to be issued. 3,36,264 shares are in the first instance offered to the existing shareholders in the proportion

of one new share to every two shares at a premium of Rs. 25 per share. The new shares will rank for dividend on the profits of the Bank accruing and earned as from 1st July, 1944. The balance of 41,208 shares will be sold by the Directors in the open market at such rates as they deem fit, but at premiums of which the minimum shall be Rs. 25 per share and the maximum shall be Rs. 100 per share.

The issue of new shares brings with it a substantial sum of over Rs 95 lakhs to the reserve fund by way of premiums. Consequently the proposed step will raise not only the capital but also the reserve, and thereby strengthens the Bank's ability to accept reasonable risks of participating in the financing of India's post-war industrial development, for which plans are now being drawn up by officials and non-officials alike. The "*Commerce*" dated 18 3 1944.

### 6. The Oriental Government Security Life Assurance Co., Ltd.

The Oriental Government Security Life Assurance Co., Ltd., Head Office : Bombay Manager : Mr. H. Edwin Jones) has completed seven decades of an undoubtedly useful career. During all these "three score years and ten," the Company has, indeed, served the people of this country well by offering protection against risk to human life. Cautious management, careful selection of lives, prompt attention to claims have all combined to make the Company one of the most popular life offices in India. To-day there are on its books as many as 540,783 policies assuring a sum of Rs. 118 crores, a record surpassed by no other Indian life office in this country.

In recent years, the Company's progress has been almost phenomenal. The business under-written by the Company, especially for the past three years, reveals that war conditions have brought in their wake unique prosperity to the "Oriental," as to many other insurance companies. The results of working of the Company for the year 1944 as compared with those for the previous two years indicate that the Company has set up several new records, despite the fact that it suffered considerable loss of business done outside India in Burma and Malaya owing to the occupation of these by Japan. The following table indicates the progress made by the Company during the past three years.

| Particulars | | 1942 | 1943 (Rs. in crores) | 1944 |
|---|---|---|---|---|
| No. of policies issued ... | ... | 36,713 | 58,012 | 87,398 |
| Sum assured ... | Rs. | 9.51 | 15.00 | 21.84 |
| Total premium income ... | " | 3.80 | 4.51 | 5.29 |
| Total No. of policies in force | ... | 4,39,940 | 4,76,039 | 5,40 783 |
| Total sum assured ... | Rs. | 88.49 | 101 05 | 117.99 |
| Claims ... ... | " | 1.76 | 1.87 | 2.16 |
| Expense ratio (per cent) | ... | 21 2 | 22.4 | 24 2 |
| Total funds ... | Rs. | 31.62 | 34.04 | 36.83 |
| Average rate of interest realised (per cent) ... | ... | 3.87 | 3.68 | 3.40 |

From the table given above, it will be seen that the number of policies issued has shot up nearly 2½ times, that is from 35,000 in 1942 to 87,000 in 1944 The sum assured has similarly gone up from Rs. 9.51 crores to Rs. 21.84 crores in 1944. The premium income in

1942 amounted to Rs. 3 80 crores, whereas in 1944 it reached as high a sum as Rs 5.29 crores. A similar spectacular rise is seen in the total sum assured of policies in force. It was Rs. 88,49 crores in 1942, Rs. 101.05 crores in 1943 and Rs. 117,99 crores in 19,42. The total fund as on 31st December, 1944 amounted to Rs. 36 83 crores which compare with Rs. 34.04 crores in 1943 and Rs. 31.62 crores in 1942.

The claims paid by the Company too show an upward trend during the three years under review as they have risen from Rs. I.76 crores to Rs. 2.16 crores. This, however, is not considered as unsatisfactory, inasmuch as the ratio of actual deaths in 1944 to those expected and provided for by the mortality basis adopted at the last valuation was 49 8 percent This compares with 48.5 per cent in the previous year.

Another feature noticeable from the table is the rise in expense ratio. This has gradually risen from 21.2 per cent in 1942 to 24 2 per cent in 1944. The increase in the year under review in the ratio of 1.8 per cent over that of the year 1943 is, according to Sir Cowasjee Jehangir, who presided over the last annual meeting of the Company, practically altogether accounted for by the increase in the first year's commission paid out in respect of the substantially increased new business of 1943 and 1944 as compared with that of the immediately previous years and to the cost of procuring the largely increased new business of 1943 and 1944 as compared with that of the immediately previous years and to the cost of procuring the largely increased new business of last year, including the expenditure on medical fees.

The gradual fall in the interest rate realised reflects the cumulative effect of high taxation and compulsory investment of the bulk of the life funds in Government securities. In order to meet the situation caused by this declining interest rate, the Company has rightly revised its tables of premium on an up-to-date basis of mortality, interest, and expenses. The " *Commerce* " dated 16-6-1945.

**7. The Industrial Investment Trust,**

It will be recalled that, in one of the previous issues of *Commerce*, we gave a brief indication of the results of working of the Industrial Investment Trust Ltd. (Secretaries: Messrs Premchand Roychand & Sons, Ltd, Bombay) during the year ended 31st December, 1943, We then stated that the year under review was one of the best the Trust had witnessed so far and that the Directors proposed to raise the rate of distribution to shareholders from 4½ per cent. per annum to 5 per cent. by paying a bonus of ½ per cent. The full report and statement of accounts, which have since been published, confirm our forecast. According to these, the Trust's profit for 1943 amounts, after providing for all expenses, as also the Secretaries' remuneration, to Rs. 4,56,259 which compares with Rs. 3,02,855 for 1942 and Rs. 2,26,323 for 1941. In other words, there has been, as compared with 1942, an increase of 1,53 lakhs or over 50 per cent. The bulk of this increase has been due to the substantial profit made on sale of investments, as witness the fact that income from this source amounted to Rs. 2,13,903, as against Rs. 55,966 for 1942. There has been an increase in income from investments too, from Rs. 2,74,195 for the previous year to Rs. 3,02,782 for the year under review. This, of course, is only as it should be, in view of the prosperous conditions experienced by practically all the industrial concerns in which the Trust has so judiciously invested its funds.

The total sum available for distribution, including Rs. 16,825 brought in from the previous year, is Rs. 4,73,084 as against Rs 3,27,912 a year before The policy pursued by the Board in regard to the distribution of this increased profit is a commendable one. The Directors have devoted—and very rightly in our opinion the major portion of the improvement in the profit to strengthen the financial position of the Trust. Thus, they have transferred no less than Rs 1,33,903 to general reserve which, a year ago, received only Rs. 50,000, and only Rs. 25,000 out of the profits for 1941. This is the first time in its history of a little over a decade that the Trust's reserves have received such a handsome allocation. With this allocation, the Trust's funds exceed Rs. 6,45,000. This, however, looks a modest one compared with the paid up capital of Rs. 50 lakhs.

The Directors have recognised the claims of the shareholders for a share in the increased profits by deciding to pay a bonus of ½ per cent, besides maintaining the dividend at the previous year's raised level of 4½ per cent. per annum. The total amount required to meet this 5 per cent. distribution to shareholders is Rs. 2 50,000 The balance left to be carried forward is Rs 88,093 which includes provision for taxation which is yet to be decided by the authorities.

A noteworthy feature as revealed by the table below is the reduction in the cash position from Rs. 6.27 lakhs to Rs. 1.44 lakhs. This is due to the fact that the Trust found fairly good scope for investing its funds and thereby raising its earning capacity substantially. It is noteworthy that the approximate valuation of the Trust's Investments (at market quotations as on 31st December, 1943, or, in the case of investments where no quotations were available, on the date the latest quotations were received,) was higher than the book value.

As regards the finances of the Trust, the following set of figures will be read with interest :—

| | As at | | |
|---|---|---|---|
| | 31-12-1943 | 31-12-1942 | 31-12-1941 |
| **Assets** | Rs. | Rs. | Rs. |
| Investments ... | 59,01,073 | 53,33,125 | 51,38,596 |
| Interest accrued ... | 37,780 | 26,354 | 28,864 |
| Future sales ... | — | 1,16,702 | ... |
| Cash ... | 1,44,521 | 6,27,218 | 5,58,670 |
| **Liabilities** | | | |
| Capital ... | 50,00,000 | 50,00,000 | 50,00,000 |
| Reserves ... | 6,45,927 | 5,08,076 | 4,50,000 |
| Reserve for taxation ... | 60,900 | 60,900 | 40,451 |
| Future purchases ... | ... | 2,78,633 | ... |
| Liabilities ... | 2,90,043 | 2,39,510 | 2,10,953 |
| Carry forward ... | 88,093 | 16,824 | 24,728 |

The details given by the Directors in their report to the shareholders about the composition of the Trust's investments reveal the following noteworthy features :—

1. There has been a further reduction in investments in sterling securities. Thus, the percentage of the latter to the total investments at

the end of 1943 was only 6.75, as against 10.52 a year ago and 13.73 two years before.

2. There has been a perceptible change in the proportion of ordinary stocks *vis a vis* the preference shares and Government securities to total investments, as the following comparative table will testify."

| | (Percentage to total investment) | | |
|---|---|---|---|
| | 1943 | 1942 | 1941 |
| Ordinary stocks ... | 57.43 | 62.47 | 61.60 |
| Prelerence shares ... | 24 79 | 26.67 | 26.46 |
| Government securities ... | 17.78 | 10.86 | 11.94 |

It will he seen that there has been a snbstantial increase in the holdings ol Government securities, mainly at the expense of ordinary stocks and only partly ol prelerence shares.

3. The increase ln the holdlngs of Government secnrities wonld appear to be due to the large acqnisition ol 3½ per cent. Government Paper. This assumption is warranted by the lact that, whereas this loan had not heen incloded in the Trnst's portfolio in 1942 lt now finds a place therein. Il the management had acqnired this loan early in the year, as we presnme it mnst have done, there would he snhstantlal capital appreciation.

4. The fall in ordinary stocks, we believe, mnst have been due largely to the liquidation of a part ol its holdlngs of cotton mlll shares many of which saw record high levels in May last. In this connectlon, lt may he of interest to note that the percentage ol cotton mlll shares to total investments at the end ol the year nnder review was only 12.52 as against 18.54 at the close of 1942 and 12.68 two years ago. Soch a qnick change ln the portlolio soggests that the Board mnst have felt that there ls not mnch room for further capital appreciatlon.

5. There have been slight decreases in the holdings ol scrlps ol banks, insurance, cement, rnbber, pnblic ntilities, and shipping, while steel, paper, railways, and sngar disclose a small increase.

As was pointed out in an earlier issue, the Directors have decided to call np the uncalled balance of Rs 50 per share and notice to this effect, it may be recalled, was published in onr last week's issue. When those calls are completed, the paid-np capital of the Trust will go np from Rs. 50 lakhs tn Rs. 100 lakhs. This will enable the Board to add many a lucrative scrip to its investment portfolio.

The "*Commerce*" dated 25-3-1944.

# APPENDIX

## The Capital Structure of Public Companies

It is very essential that the promoters and organisers of industrial ventures should prepare the capital structure of their companies in such a way as to create confidence amongst investors and to avoid repetition of the mistakes that were committed by industrialsts in the inter-war years, some of which have cost the investors heavily. Much of this could have been averted had only the capital structure of companies been kept simple, and the capital requirements properly assessed. Reproduced below, from the *Commerce* dated 25th November and 2nd December 1944, is an excellent article on this subject by Mr. P. Chandra, M.A., who discusses in a very interesting manner the faulty character of capital structure of companies in the past and provides a convincing case for simplification.

An analysis of the financial affairs of several companies during the slump years shows how shareholders and directors alike failed to recognise how much of their adversity was due to faulty capital structures. It also comes to light that the main sufferer almost always is only the ordinary shareholder. Now, ordinary capital forms the bulk of public investments in joint stock companies. The ordinary shareholder is said to be the backbone of a company. If India is to proceed a pace in its programme of industrialisation by joint-stock enterprise, every effort must be made to strengthen this backbone. Unless our future capital schemes give more safety to the ordinary capital, it may not be too easy to find all the money needed to finance the schemes which may be under way in the post war period. Shyness of capital is connected with the safety of capital. And it must be understood that capital here is not shy only because Indians are fond of laying by gold bars, but also because an average Indian regards such investment with an eye of dread as pure speculation.

Joint stock companies in India combine ordinary shares either with cumulative preference shares, or with deferred shares, or with both. Some companies have participating and redeemable preference shares. Companies also have sometimes some capital in the form of debentures. We have to see by examining the capital structures of a few companies and their behaviour in the past, the merits and demerits of each combination.

### (1) Combination with Cumulative Preference Shares

Cumulative preference shares are, in common belief, issued to provide an investment opportunity to the cautious investor who wants a steady income and safety of capital. The past record, however, of Tata Mills (Managing Agents :-Messrs. Tata Sons Ltd.), Elphinstone Spinning and Weaving (up to 1943 Messrs. E. D. Sassoon & Co.), New

Victoria Mills (Sir J. P. Srivastava and Sons), India United Mills (up to October 1943 Messrs. E. D. Sassoon & Co.), Bradbury Mills (Messrs. Ramnarain Sons Ltd.) Kesoram Cotton (Messrs. Birla Bros Ltd.), Craig Jute (Messrs. Beg Dunlop & Co., Hastings Jute (Messrs. Andrew Yule & Co.) Hukumchand Jute (Messrs. Ramdutt Ramkissendass), Soorah Jute (Messrs. Mcleod & Co.), and Kumardhubi Engineering Works which have part of their share capital in cumulative preference shares, proves conclusively that, in times of a slump, the cumulative preference share is a curse to the company and to its holder. The accumulated preference dividends of Tata Mills, Elphinstone, India United, and Kumardhubi Engineering works could be wiped off only by transferring substantial portions of the ordinary capital of the preference shareholders. The preference shareholders of New Victoria, and Craig Jute saw the spectacle of cancellation of their accumulated dividend in exchange for a pittance. The Hastings Jute, Bradbury Mills, Hukumchand Jute, and Soorah Jute are still labouring after four years of boom, to pay off the accumulated preference dividend so that they may not sacrifice their ordinary capital. Here, the accumultated dividend is coming in the way of a dividend to the ordinary shareholder. Examples can be multiplied. but these are some, in which front-line directors and managing agents had the dispensation of the company's funds.

Three facts emerge on a careful study of these companies. These are :—

1. In certain circumstances, the cumulative preference shareholder may have neither steadiness of income nor safety of capital. The very provision for accumulation of dividend is nugatory to the idea of steadiness. When dividends begin to accumulate, the steady income is gone and gone also with it is the safety of the capital, because even a preference share has value only as a dividend earning security As prospects for realisation of dividend recede, the price of the share also dwindles. The original holder sells off at the best reduced price. The fact that the shares change hands is very important. Even though, after 20 or 25 years, the Company may begin to pay the preference dividend, the fact remains that the original holder lost both income and part of his capital. When the happy occasion to get a return on the preference shares comes after a lapse of years, it will be found that nearly all the preference shares are concentrated in the hands of a few persons, the directors, managing agents and their friends, who corner them, sometimes at dirt-cheap rates, in anticipation of the coming windfall. In this, no fault could be ascribed to the directors or the managing agents. Prices declined according to the trade cycle But where the responsibility of the directors, etc., lies is in creating the mistaken belief that the cumulative preference share can earn a steady income always or that it will maintain its value even in dear money conditions. The delusion has been there for a long time, and the sooner it is dispelled the better.

2. The dividend accumulated in lean years becomes a charge on the ordinary capital of the company. The Indian Companies Act has this strange anomaly, that it does not allow disbursement of interest without permission ; yet it allows the interest to accumulate and become a charge on the capital. The Kumardhubi Engineering works, Ltd., appeased the preference shareholders by giving them 7/10ths of the ordinary capital ; the Elphinstone Spinning gave half the ordinary

capital. If the ordinary shareholders do not agree to this sacrifice, they may be more or less permanently debarred from getting anything, as is happening in the case of Bradbury Mills, Hukumchand, and Hastings Jutes

3. Although the accumulated dividend is a dead loss to the company, which has to be paid from the ordinary capital and which sometimes involves sacrifices from the preference shareholder as well, the Government does not treat it as loss in business for purposes of setting off from future years' profits. This means that the company is unable to take advantage of the provision of section 24 (2) of the Income-tax Act. For example, at the end of 1942, the accumulated preference dividend of Elphinstone Spinning and Weaving amounted to about Rs. 30 lakhs. In 1941 and 1942, the Company paid about Rs. 34 lakhs in taxes to the Government which was more than sufficient to wipe out the entire liability. The Government, however, had its taxes and the preference holders got only half the ordinary capital. This attitude of the Government, in face of the fact that such contingencies arise because of its own laws, is callous. But, so long as this attitude persists, it is better for the directors and managing agents to avoid creation of such contingencies by not having the preference share at all.

This is a bleak picture of the prefence share and surely the reader must be thinking of the other side of the medal. Tata Steel, British India Corporation Allahabad Bank, Ahmedabad Advance preference shares. About these the following observations may be made :—

1. These companies earn sufficient profits even in lean years to pay out the preference dividend regularly. If all companies were to earn profits like these companies, there would be no harm in having cumulative preference shares, because then the necessity to accumulate dividends will not arise. However, the number of such companies is not large and they may be counted on the fingers.

2. In slump years, up to 1935 even Tata Steel did not pay any dividend to the ordinary shareholders All the earnings were absorbed by the preference dividend. The B.I C. had many internal upheavals in the early thirties because of preference dividend.

3 There is no doubt that, in periods of boom or monetary inflation like the present, the preference shareholder does not share the prosperity of the company with the ordinary shareholder and thereby enables a higher dividend possible to the ordinary shareholder. But this advantage is temporary and only helps to make the ordinary share more speculative. Moreover, the higher dividends in periods of boom are not sufficient to set off the losses suffered in times of slump. Take, for example, the Associated Hotels and Spencer & Co. In the slump years these companies earned sufficient profits to pay off the preference dividend and 1 to 2 per cent. on the ordinary capital. Now, in the boom period, their dividend has not gone beyond 10 per cent. which is poor compensation for the low dividends which the ordinary shareholder got because part of the capital was preferential.

When all is said and done, it will be found that it is very undesirable to have cumulative preference shares, unless the company's profits cover their dividend at least two times, and unless the company is passing a period of boom. New companies which are being started for expanding industry in the post-war period should not have preference

capital, firstly because the interest which the company will receive on its investments from the Government will be sorely needed for explora tory purposes and secondly, because the profit margins of these indnstries in the slump period next following is not calculable now.

(2) Combination with Deferred Share

The deferred share is fonnd sometimes in combination with ordinary shares alone as in the India United Mills and the Indian Steel and Wire Products bot more often it is fonnd in combination with both ordinary and preference shares. The deferred capital is always a small fraction of the ordinary capital. The Tata Iron and Steel deferred share is the most famous of its class. Other companies having this combination are the Aluminium Corporation of India, Indian National Airways, Dalmia Cement, aod New Victoria Mills.

The ordinary shareholder fares the worst in these compaoies. While the prefereoce dividends absorb most of the company's profits in adversity, in prosperity the deferred share takes away a large portion of the profits The presence of the deferred share makes the ordinary share doubly speculative. It creates a tendency in the minds of the directors and managiog agents to dissipate the earned profits of the company by declaring large divideods on ordinary shares so that dividend on the deferred shares may be huge. Or, if the profits are not large enough to warrant a dividend on deferred shares, they withhold the dividend on the ordinaries. The worst defect however, is that the involved character of rights between the different classes of shares hampers progress and undoes efforts at simplification of the share capital. The Aluminium Corporation of India, Dalmia Cement, and Indian National Airways are of recent origin and it is too early to comment oo them. *The Tata Iron* and *Steel* and *New Victoria* however, can be studied with benefit.

The following table aboot the resnlts of the Tata Iron and Steel will be fonnd usefol .—

| Year | Profit | Depre-ciation | 'Ordinary' dividend | 'Deferred' dividend | Reserve Fund | Additional saviog if the dividends of 1939 had been paid in *subsequent* years also |
|---|---|---|---|---|---|---|
| | Rs. | Rs. lakhs | Per cent | Per cent | Rs. lakhs | Rs lakhs |
| 1936 ... | 244,02,496 | 98 | 8 | 25 | ... | ... |
| 1937 ... | 256,81,171 | 93 | 13 | 120.7 | ... | ... |
| 1938 ... | 329,39,339 | 88 | 20.66 | 252.4 | ... | ... |
| 1939 ... | 364,81,092 | 100 | 24 | 312.1 | ... | ... |
| 1940 ... | 357,39,506 | 50 | 33.66 | 464.8 | 80 | 49 |
| 1941 ... | 462,84,521 | 150 | 38.66 | 575.2 | 75 | 77 |
| 1942 ... | 472,83,925 | 125 | 36 | 527.4 | 100 | 63 |
| 1943 ... | 357,98,618 | 125 | 30.66 | 431.8 | 35 | 37 |
| | | | | Total ... | 290 | 226 |

It will be seen that the dividend result in 1940 was achieved only after curtailing the depreciation to Rs. 50 lakhs, which represents only 1.61% of the block capital of Rs. 31 crores. The Company also has some wasting assets Therefore, the depreciation was certainly inadequate. Again, if the directors had mastered the temptation of declaring larger and larger dividends on the deferred shares and had maintained the dividend figures about those of 1939, the Company would have accumulated a sum of Rs. 226 lakhs which would have been a real reserve fund for the Company, because all the depreciation and reserve fund hitherto accumulated by the company is already invested in the existing block. The said Rs, 226 lakhs would have enabled the managing agents to extend the works without the necessity of outside finance. It would, moreover, have kept the appetite of the deferred shareholder within bounds and would nave prevented him from standing in the way of the conversion scheme. On the basis of dividend proprotion, it is reported, the managing agents wish to convert the deferred capital into ordinary by allotting five and a half shares ordinary for every deferred share. The deferred shareholder, however, demands his pound of flesh. On the basis of rights accruing to him on the liquidation of the Company, he is entitled to 60 per cent. of the surplus assets remaining after payment of the share capital. This entitles him to about seven and a half ordinary shares. It looks very hard on the ordinary shareholder, although, in the case of this Company, the managing agents rather than the ordinary share. holders, are the mainstay of the Company. The credit for the increased earning power of the Company rightly belongs to them. As the facts stand, the deferred shareholder with only, less than Rs.15 lakhs of capital wishes to make himself master of the lion's share in a block of Rs 31 crores, and defies all attempts at simplification of the capital structure without which there can be no increase in capital.

New Victoria's past is a record of financial jugglery, although the reduction and increase in the capital seem to be intelligent and opportune. But even the opportune reduction of capital in 1930, just before the first year of depression was of no avail. The Company was unable to pay preference dividends regularly and no dividend was paid on the ordinary and deferred capital until 1941, when the huge dividend of 20 per cent. on ordinary and 130 per cent. on deferred shares was paid This dividend was made possible, because the annual profit which was normally Rs.2 to Rs. 3 lakhs, rose suddenly to Rs. 10 lakhs in 1941. Not only did the directors pay the high dividends, they also thought it fit to increase the capital of the Company by about half on the basis of the temporarily increased profits. Every one knows that the high profits will not remain long. In fact, mopping up has begun already. There is no increase in the productive capacity of the mills. One would, therefore, expect either another reduction of capital or extinction of dividends at the beginning of the next slump. A Company whose profits are subject to such wide fluctuation should not have preference and deferred capital, because the fluctuation is naturally transferred to the price of the shares.

**Companies with Ordinary Capital Only.**—Companies having only ordinary capital can be roughly divided into two classes: (i) A company in which the subscribed capital bears a considerable proportion to the block cost, e. g., Associated Cement, Model Nagpur, Apolo Mills, Champdany Jute, Megna Jute, etc., (ii) A company in which the subscribed capital forms only a small fraction of the block cost, e.g., Bombay Dyeing

Centnry, Coimbatoie, Bangalore Woollen, Orient Jute, and nearly all the mills of Ahmedabad.

The Associated Cement Companies Ltd.. is in the hands of able and trosted directors. The Company is trying to manufacture in its own workshops plant and machinery for further development of the ceramic industry, so that, in fnture, costly machinery may not be imported from abroad. It may be remarked that this in one of the few companies which have not been benefitted by the war. It was better off in 1938, when, out of a total profit of Rs. 132 lakhs, it conld retain for depreciation and other appropriations Rs. 111 lakhs. In 1943, out of Rs. 145 lakhs, the Company could retain only Rs. 97 lakhs. This result is not particularly enconraging when it is remembered that at least half a dozen of the Company's factories are in States where no E.P.T. has to be paid. The effects, of course, is due to the miserably low margin of profit which the Government pays on the bnlk of the production which it purchases As the capital of this Company is nearly eqnal to the block cost and the whole of it is ordinary, the dividend result ot this Company is not spectacular. It could be easily improved by having only half the capital in ordinary shares aod the rest in 4 per cent. debentnres

Megna Jute and Model Mills, are two examples of companies started in the boom period, 1920. which paid colossal sums for machinery which was later found to be cheap. Jute companies which purchased machinery in 1919 20 lost half their block cost in 1929-30. Megna Jote had the foresight in 1934 to write off the huge initial loss on block accoant by rednncing the capital from Rs. 62 lakhs to Rs. 25 lakhs. Model, Nagpnr, is the costliest among costly cotton mannfacturing plants, but it has not redneed its capital. In fact, these are not the only companies which have a high block cost. The fact was early recognised by Indian business men that they had to pay extravagant prices for plant and machinery to their snppliers abroad, and it was in consequence that they devised the method by which they kept the dividend-earning capital at a very small fraction of the block cost and met the rest of the colossal expenditnre by long-term deposits on fixed rates of interest or by issuing debentnres. The first method of finance was peculiar to the Ahmedabad millowners who sometimes also gave a share in the managing agency for certain fixed amount subscribed privately towards the block cost

### (3) Combination With Debentures

This method is followed, among others by the Sholapur Spinning and Weaving Mills and the Indian Iron and Steel. These companies have backed their ordinary capital with hnge debenture capitals at low rates of interest. This is the most important combination and the simplest.

It is well known that debentnres are not usually dealt with in the market. Why? Becanse they are tightly held by the banks, insurance, and investment companies. The reason for which these bodies firmly hold their debentures is that the debenture really possesses the many virtues which the preference share only seems to possess. Like the preference share, they are fixed interest securities but they have the additional advantage that, if the interest is not paid regularly, the debenture trustees may have the assets of the company auctioned if they like. The debenture is almost always redeemable at a known date. This stabilises the price of the debentnre although

there is even then a price mnvement with changing monetary conditions which is, however negligible. One is always sure to get back his capital after some time. Thns, debentnres give the greatest security of capital. They have some additional advantage also. The accumulated interest on debentnres is considered by the Government to be loss in business for purposes of Section 24 (2) of the Income tax Act. The advantage which the preference share affords to the ordinary shareholder in times of boom by making larger dividends possible to him is conferred by the debentnre in a greater degree because the rate of interest on debentnres is lower than that on preference shares. For the same reason, the liability of the company for paying interest in times of slump remains lower than in the case of preference shares.

All these advantages occur to mind at once. However, there is another snbtle advantage also which the debenture possesses. The existence of debentnres as part of the capital keeps a healthy check on the extravagance of the managing agents and limits the loss of the company. If the loss exceeds a certain limit, the debenture trustees, if they are vigilant and are not in the pay of the managing agents, will at nnce pounce upon the company. thus saving it from further loss.

Take the case nf Apollo Mills. In 1939, the Managing Agents of Company made it liable to themselves tn the extent of nearly double its subscribed capital. In that year therefore, the nrdinary capital was reduced from Rs. 25 lakhs tn Rs. 1 lakh and new shares worth Rs. 49 lakhs were issued to the Managing Agents in virtue of their advances to the Company. Thns, they acquired a 98 per cent, Interest in the Company. If, however, instead of taking a loan from the agents, the Company had issued debentnres, it would not have gone to snch depth. In the first place, the knowledge that the debentures form the first charge on the assets of the Cnmpany would have deterred the Managing Agents from making the Company so heavily Indebted to themselves. Further, long before the Company came to these straits the debenture holders wonld have asked for the dissolution of the Company and thus saved for the shareholder a bigger share than he got in 1939 in the reconstitnted Company and probably also would have got rid of the Managing Agents.

**Need for safeguards :**—There are certain safegnards in investing In debentnres which must be carefully observed. The first is that the debenture issne must be secured by the fixed, not floating, assets of company or by unpaid liability of the shares. A company having a wasting asset, e. g., coal company, should not issue debentures nnless they are redeemable in about half the life of the asset. The second essential is that the debentnre trustees should not be in the pay of the directors or managing agents and mnst consider the interest of the debentnre-holders. The third essential is that the interest on debenture capital must be fully covered by the earnings in the case of an existing company and there must be reasonable prospects of such earnings in the case of new companies. The debentures must have a provision for redemption. The trust deed mnst be carefully drawn up and must not leave loopholes

Companies like the Associated Cements and Model of Nagpur will benefit immensely if they return some of their ordinary capital and issne 4 per cent debentures instead. These should be redeemable in

seven or eight years by means of a sinking fund. If, out of the capital of Rs. 7 crorers in the Associated Cements, only Rs. 2 crores were converted into debenture stock, the Company would be saving 3 to 4 per cent. on this amount as well as the income tax on this saving. If the company does not pay out this sum to ordinary shareholders, it will conserve about a crore of rupees in eight years.

There are two dangers in debenture capital. The investor usually regards an issue of debentures as a sign of the bankruptcy of the company. This view is not correct. By issuing debentures, a company raises the cheapest capital, while giving the greatest security. The other danger is that the directors can make even a debenture as speculative as the ordinary share. There are two fine examples of this in Tata Chemicals and Steel Corporation of Bengal. Both these companies give the debenture holders the right to convert it into ordinary shares. It is not clear what advantage accrues to the company except that the directors are absolved of the responsibility to earn sufficient money to redeem them within time.

Such right to conversion operates against the interest of the ordinary shareholder. Both these companies could have easily raised at the start additional ordinary capital equivalent to the debenture capital, thus saving the interest paid on the debenture capital. The ordinary shareholder suffered then. Now when the time for the ordinary shareholder to earn a dividend arrives the debenture holder becomes an ordinary shareholder and entitles himself to the profits which rightly belong only to the original ordinary shareholder. Thus the ordinary shareholder suffers again. But that is not the end. The position of the company becomes financially unsound. The capital becomes unnecessarily watered. To take the example of Tata Chemicals during 1943, out of the debenture capital of Rs. 35 lakhs, debentures worth Rs. 26,16,600 were converted into ordinary shares worth Rs. 20,93,280 at the rate of 8 ordinary shares for every debenture. The existing ordinary capital was Rs. 64 85,300 The capital was therefore, increased by one third. The ordinary share was quoting those days about Rs 35, so that for every debenture of Rs. 100 the holder received securities worth Rs. 280. The debenture itself was being quoted about that rate. Similarly, in the Steel Corporation of Bengal, every holder of debenture worth Rs. 660 could have it converted into 40 ordinary shares now worth Rs. 1,120. The latest quotation of the debenture was £152. In such schemes, although the debenture holder benefits greatly if the company's performance is profitable and the ordinary share quotes at a premium, the financial soundness of the company is impaired and the ordinary shareholder suffers a loss quite disproportionate to the benefits, if any, which he might have previously derived from the existence of the debentures. Happily for us, such examples are only few.

**Watering of Capital.**—Capital structures technically have been covered in what has been written, but no study of this subject can be complete without considering the watering of capital. In a period of boom, this occurs frequently. In some cases, it is necessitated by circumstances; in others, it is indulged in for sheer bravado. In the latter case, it turns out to be harmful to every one except the directors and managing agents. The capital should not be increased unless the earning power of the company increases permanently.

In 1943, a number of companies increased their capitals. Two of them are worth mentioning, because they show up what is worst in unnecessary changes of capital. The Cawnpore Textiles has, since 1927, four changes of capital to its credit, the last being in 1943, when it doubled its capital from Rs. 7,50 000 to Rs. 15,00,000. For the half-year ended September 1943, the Company paid a dividend of 40 per cent on the watered capital bnt it has announced for the half-year ended March 1944, a dividend only of 15 per cent Their bravado seems apparent from the remark which the directors have made in their report that in future dividends 'must" be limited. What a shock it must be to the investor and what complete lack of foresight the directors, etc., showed in watering the capital ! Again, there is the case of Alcock Ashdowns which also watered its capital to double its ordinary capital. This year the company has declared a dividend of 10 per cent. as against 20 per cent. last year. The Company could not get even an interest allowance from the Government for its increased capital under the E. P. T. regulations. If the investor had himself invested in Defence Bonds, the Government would have allowed him 3 per cent. interest. The fun becomes apparent when it is remembered that each additional share of Rs. 100 was issued at a premium of Rs. 100.

THE END

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